RAILROAD CONSOLIDATION: SMALL BUSINESS CONCERNS

JOINT HEARING

BEFORE THE

COMMITTEE ON SMALL BUSINESS
HOUSE OF REPRESENTATIVES

AND THE

COMMITTEE ON SMALL BUSINESS
UNITED STATES SENATE

ONE HUNDRED FOURTH CONGRESS

FIRST SESSION

WASHINGTON, DC, NOVEMBER 8, 1995

Printed for the use of the Committee on Small Business

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RAILROAD CONSOLIDATION: SMALL BUSINESS CONCERNS

WEDNESDAY, NOVEMBER 8, 1995

HOUSE OF REPRESENTATIVES, COMMITTEE ON SMALL BUSINESS AND U.S. SENATE, COMMITTEE ON SMALL BUSINESS, WASHINGTON, DC

The Committees met, pursuant to notice, at 2 p.m., in room 1100, Longworth House Office Building, the Honorable Jan Meyers (chair of the House Small Business Committee) and the Honorable Christopher S. Bond (chairman of the Senate Small Business Committee) presiding.

Chair MEYERS. The hearing will come to order. At the outset of the hearing I would like to welcome our colleagues from the Senate to the House side of the Hill for our joint hearing today. The subject of today's joint hearing is railroad mergers and their impact on small business, particularly small shippers.

Not too long ago, in 1980, there were 42 Class I railroads operating in this country. If the mergers already approved, announced or heavily rumored this year are completed, there will be only eight Class I railroads left in this country. At the beginning of this year, there were 12.

Please do not mischaracterize my concern. I am sure that many of the Class I rail mergers that have occurred in the past 15 years were not only necessary but were clearly procompetitive.

Our primary concern for today's hearing is the recent trend toward megamergers among previously competing Class I railroads and how these megamergers affect small business shippers, particularly shippers of bulk commodities such as agricultural goods.

As our first witness we have with us today is a former colleague and a fellow Kansan, Secretary of Agriculture Dan Glickman. After Secretary Glickman's testimony we will have a brief round of questioning. Following our questioning of Secretary Glickman, we will hear from our second panel today, and we will have eight witnesses on our second panel, who are intimately familiar with the issue of large rail mergers and how they impact small shippers.

One small housekeeping matter before we begin. Chairman Roberts of the House Committee on Agriculture is unable to be with us today. He would like to submit a statement for the record and without objection I will do that.

[Mr. Roberts' statement may be found in the appendix.]

Chair MEYERS. Furthermore, without objection I would like to keep the record of this hearing open for 10 days to receive statements of other colleagues and other interested parties who are not with us at today's joint hearing.

At this time I would like to recognize my colleague, Senator Bond, for an opening statement.

Chairman BOND. Thank you very much, Madam Chair. I'm pleased to join you once again as a co-chair of a joint hearing of the House and Senate Small Business Committees. I express thanks for your gracious hospitality. Just last week we held a very successful joint hearing on our side of the Capitol on the cost of regulation on small business.

With today's hearing the Senate is able to reciprocate and join you here on the House side in this very lovely hearing room of the House Ways and Means Committee.

Today's joint hearing focuses on the impact of rail mergers on small shippers. It demonstrates the shared concerns of many in the House and Senate Small Business Committees with maintaining competitive rail service for small shippers. This is very much an outside-the-beltway issue.

Again, Madam Chair, I thank you very much for your hospitality and also for your quick lesson in electronic high technology. Obviously the House does more things electronically than we do and I appreciate your good guidance.

We're here today to listen to small shippers and learn from their unique perspective on recent and proposed rail mergers. Most of our witnesses have traveled here especially to testify before the Committee and I join our distinguished Chair in welcoming all of you to Washington.

Madam Chair, several weeks ago I was back home and went to Trenton, Missouri, and I had a chance to talk with Frank Hoffman, who owns and operates a family run grain elevator. Frank expressed to me his very real concerns about the cost and quality of rail service and how rail mergers were affecting or could affect rail service to his elevator.

It was very clear from our talk, and from conversations I've had with others like him, that these issues not only affect the elevator operators like Frank, but the hundreds of farmers who depend upon the local grain elevator to get their corn, soybeans, and wheat to market and on many other small businesses who also depend upon good rail service, readily available at reasonable cost, to transport their raw goods and their products out.

The situation of Frank Hoffman is typical of grain elevators throughout Missouri and much of the Midwest. Many of these elevators are totally dependent on rail transportation to get their product to market and to import fertilizer at competitive rates.

Today the Committee is going to get a chance to hear more about the effects of rail mergers on a typical small-sized grain shipper, and the testimony is going to come from Phil Hoffman, Frank's nephew. Phil, I welcome you to the Committee. I look forward to your testimony.

Since my initial conversation with Frank Hoffman back in Trenton, I've heard from many other small shippers who are worried about rail service and the impact that mergers and other consolidations will have on their service. These small shippers have a vital interest in maintaining high quality, competitively priced freight rail service in this era of megamergers in the rail industry.

While they recognize, as the chair has already pointed out, that many of these mergers present opportunities for more efficient rail service, they're also concerned that these mergers may adversely affect small shippers. I hope today's witnesses will provide the Committee with a clear picture of both the potential benefits and the problems presented by these mergers.

Madam Chair, I'm delighted to be able to join you today to provide the small shippers this opportunity to bring their concerns to the attention of Congress. We particularly welcome the presence of our distinguished Secretary of Agriculture, who can provide us a broader perspective on the impact these mergers may have throughout the agricultural community in America today. Thank you, Madam Chair.

Chair MEYERS. Thank you, Senator Bond. At this point I would like to recognize the ranking member of the House Committee, Mr. John LaFalce of New York.

Mr. LAFALCE. Thank you very much, Madam Chair. I have an opening statement and if you won't object I'll ask that it be included in the record as if it were read.

Chair MEYERS. Thank you.

Mr. LAFALCE. Ill simply say I'm delighted to have our friend and colleague, Secretary Glickman, here before this joint hearing. I look forward to his testimony and the testimony of others.

[Mr. LaFalce's statement may be found in the appendix.]

Chair MEYERS. Senator Wellstone.

Senator WELLSTONE. Thank you. Given the tremendous pressure I've just been under up here, I have no long opening statement. Mr. Secretary, we'll get right to you.

Madam Chair and Mr. Chairman, thank you for this hearing. It's very important. I just would ask that my full statement be included in the record, my full statement be included in the record, and I want to just highlight the fact that I want to have a statement included from the Farmers Elevator Association of Minnesota and also a set of articles or series of articles written for the Des Moines Register by George Anthan just a couple of weeks ago which I think goes right to the heart of this issue.

If we could, Madam Chair and Mr. Chairman, include that in the record, I would be very pleased.

Chair MEYERS. Without objection.

[The information may be found in the appendix.]

Senator WELLSTONE. We're not talking about Adam Smith's free enterprise economy here that the farmers are faced with, and I think this is an extremely important hearing. I thank you.

Chair MEYERS. Thank you, Senator. Without objection, all opening statements will be included in the record, and I see that Senator Bumpers has arrived and I'd ask him if he has an opening statement.

Senator BUMPERS. I have and I'd be delighted to submit it for the record, Madam Chair.

Chair MEYERS. Senator Bumpers will submit his statement for the record so we will proceed to hear Secretary of Agriculture Dan Glickman.

TESTIMONY OF THE HONORABLE DANIEL R. GLICKMAN, SECRETARY, U.S. DEPARTMENT OF AGRICULTURE, ACCOMPANIED BY PAUL KEPLER, DEPUTY DIRECTOR, TRANSPORTATION AND MARKETING DIVISION, AGRICULTURAL MARKETING SERVICE

Secretary GLICKMAN. Thank you, Madam Chair and Senator Bond. It is an honor for me to be here. I recall on a few occasions I appeared in this room as one of your colleagues, and I'm delighted to be here in my capacity as Secretary of Agriculture with Mr. Brownback. I'm most appreciative of this opportunity.

I'm pleased to be here to discuss small business concerns with the increased consolidation of the railroad industry. With me today is Paul Kepler, Deputy Director of the Transportation and Marketing Division of USDA's Agricultural Marketing Service. I appreciate the Committee's interest in this important issue and ask that my entire written statement be entered into the record.

Perhaps more than any other industry, American agriculture is fundamentally dependent on having an affordable, cost-effective railroad system. While American farmers bear the ultimate burden, over 10,000 local country grain elevators and dozens of regional and local railroads also depend on access to major railroads in order to be profitable.

I want to say, Madam Chair, that my remarks do not reflect any formal position on any merger, whether it's the UP–SP or any other merger. But from my perspective, in the context of American agriculture, I am very concerned with the growing concentration in the railroad industry. If the proposed merger of the UP–SP is approved, there will be only two major Class I railroads serving the entire Western United States.

Mergers do provide some increased efficiencies in railroads and elsewhere. Nevertheless, this merger could have a profound effect on agriculture and the entire rural economy. By reducing the level of competition, the proposed merger could have serious implications for the rates and availability of rail transportation for the agricultural industry.

For example, the USDA's Economic Research Service issued a report in 1989 which concluded that competition among railroads has a strong effect on rates for agricultural shippers. As competition increases, rates go down. As concentration increases and competition is reduced, agricultural shippers will incur higher rates, particularly those shippers who are long distances from barge transportation.

Local and regional railroads have ensured that rural rail service continues despite restructuring and abandonment of rural lines by larger railroads. As consolidation continues, these smaller railroads will likely play an even more important role in serving agriculture.

Small shippers and railroads have a number of concerns with the increased consolidation of the major railroads, including: First, a growing potential for captive shippers who are only served by one railroad; second, reduced or inadequate service; and third, noncompetitive rates.

These are legitimate concerns that must be addressed. This year, for example, there is a serious problem with rail car availability in some States—Iowa and Minnesota, for example—where a large

amount of grain is being stored on the ground. Not only will this reduce farm income as the quality of the grain deteriorates, but it is occurring at a time of record tight grain supplies.

Moreover, USDA recently released a report which demonstrated that the lack of available rail cars reduces the price a farmer receives at the local country elevator and reduces U.S. competitiveness in world markets. I'd like to submit a copy of that report for the record.

Chair MEYERS. Without objection.

[The information may be found in the appendix.]

Secretary GLICKMAN. The 1995 Farm Bill is likely to increase the importance of competitive rail service for U.S. agriculture. In addition to reducing farm program spending, the 1995 Farm Bill will likely provide U.S. farmers with much greater planting flexibility, which is one of the principal components of the administration's farm bill proposal and most of the proposals on Capitol Hill, as well. Farmers will be planting for the market, not for the farm program.

Reliable, cost-effective transportation of agricultural products enables U.S. agricultural producers and shippers to be competitive in both domestic and export markets. Indeed, one of the principal reasons U.S. agricultural exports continue to expand and compete in the world market is the transportation infrastructure that brings products from our farms and local elevators to export terminals.

To enable farmers to realize the benefits of a market-oriented farm policy and maintain continued growth in U.S. export markets, we simply must ensure the continued availability of an adequately and competitively priced railroad system.

As Secretary of Agriculture, I am committed to taking an active leadership role in working with the agricultural and transportation communities to achieve this important goal. Currently, USDA participates in the National Grain Car Council established by the ICC, and I am establishing a working group within the Department headed by Mr. Kepler, to whom I referred before, which will work to develop long-term solutions to the rail car supply problem. I look forward to other suggestions that the Committees may have regarding how USDA can address these important issues.

I thank you for holding this hearing. This is very important, particularly at a time when Government agencies are considering a variety of mergers, both ones now and perhaps in the future, and I think this hearing record will be useful in establishing the unique problems and needs that American agriculture faces in a changing world market. I thank you very much. I'd be open to any questions that you have.

[Mr. Glickman's statement may be found in the appendix.]

Chair MEYERS. Thank you very much for being here, Secretary Glickman. Let me ask, you heard me say at the beginning that in 1980 there were 42 Class I railroads. This has come down to 12 at the beginning of this year and if all mergers, either rumored or announced, take place, there will be 8.

Are you aware that the mergers of the last 10 years have impacted negatively on the ability of farmers and small shippers?

Secretary GLICKMAN. Well, some of the studies that I referred to talk about availability of grain cars, the supply of grain cars, how

railroads transport cars in a modern world, and the increased use of unit trains. I think that you have seen, as railroads have grown larger and larger, a different methodology of making money and the greater likelihood of serving large volumes. I think that that has had some impact on availability of the cars and rates.

I don't have anything in hand to tell you specifically that farmers are worse off now than they were 10 or 15 years ago. I can tell you that there have been fairly extensive abandonments as a result of mergers, but some of those abandonments have been picked up by smaller, short-line-type railroads, and so the service has continued to be provided in some areas.

But to most farmers, particularly grain farmers, the rail system is the only real feasible way of shipping. Trucking is not terribly feasible in shipping grain. So, the mergers have had some impact, which has been experienced as much in the availability of cars as anything.

Chair MEYERS. Thank you, Mr. Secretary.

Senator Bond, do you have questions?

Chairman BOND. Thank you, Madam Chair.

Mr. Secretary, you mentioned the potential problems facing the smaller railroads and their shippers. How much of the agriculture sector relies on the smaller railroads and how much depend upon small grain elevators? I doubt that this is information readily at your fingertips but if the Department could provide us, for the record, some information on that, it could be very helpful.

Secretary GLICKMAN. I will get you that information. I will tell you that I don't have it in that context. I can tell you that the way the issue is defined in the Department, and we'll give you the additional information.

Any shipper capable of shipping 25 cars or less is considered a small shipper. Now, this is not the size of the railroad. This is the size of the shipper. These are the shippers that are calling USDA for assistance. We rarely have calls from shippers moving 75 or more cars. They tend to be moved in larger unit train-type arrangements.

Based upon our review of the 1993 data, these smaller shippers of 25 cars or less originated about 45 percent of all grain shipments. Now, that doesn't deal with the specific question you asked, which we will provide you.

Chairman BOND. If that information is readily available, it might be helpful. Obviously I know that it may be difficult to get those statistics.

Thank you, Madam Chair.

Chair MEYERS. Thank you.

Mr. LaFalce.

Mr. LAFALCE. Madam Chair, I have no questions.

Chair MEYERS. Senator Bumpers.

Senator BUMPERS. Thank you, Madam Chair.

Mr. Secretary, you mentioned how many railroads we have now compared to 1988, a reduction—I forget exactly what your testimony was; what was it?

Secretary GLICKMAN. I think it was Mrs. Meyers who said that.

Senator BUMPERS. What was the number, Mrs. Meyers? Do you remember?

Chair MEYERS. This is the number of mergers? Is that the question you asked?

Senator BUMPERS. No, it was the number of railroads—I forget exactly the term.

Chair MEYERS. The statistic that I gave was that in 1980, there were 42 Class I railroads and that at the beginning of this year there were 12 and if——

Senator BUMPERS. That was the figure.

Now my question, first of all, Mr. Secretary, were you aware of that?

Secretary GLICKMAN. I was aware of the consolidation but I'm surprised, frankly, by the profound change in the numbers in the last 15 years.

Senator BUMPERS. Well, perhaps you're not the right person to ask and maybe somebody else will know the answer and will have thought about it. I'm just curious as to what impact that's had on competition, what impact that's had on small shippers, which is what this Committee's principal concern is.

Secretary GLICKMAN. Well, I think that it's had some impact on rates and availability of cars and we have some reports that talk about it. Some of it's regional. Some of it tends to affect the upper Midwest more, because of the nature of corn production and the fact that during the wintertime it's hard to ship on barges. But it's clearly had some effect.

Senator BUMPERS. Well, of course, the normal and natural consequence of mergers is, first, job loss. That's one of my concerns. That's not the subject of this hearing but it's a major concern of mine.

Second, of course, is the impact it has on competition and therefore, the ability of the railroads to raise rates. We're an agricultural State, as is your own home State, and of course, that's a major consideration for me personally. I think there will be other people here perhaps who can give us a little historical background as to what's happened in the past.

So, with that, Madam Chair, I have no additional questions.

Chair MEYERS. Mrs. Smith.

Mrs. SMITH. I think I'm just anxious to hear the testimony.

I appreciate yours, Mr. Secretary. I hadn't heard you speak before. Thank you.

Secretary GLICKMAN. Thank you.

Chairman BOND. Senator Wellstone.

Senator WELLSTONE. Thank you, Mr. Chairman.

Mr. Secretary, two quick questions. You mentioned Minnesota. In my State the two issues are the availability of transportation and the cost. We now have this effort, with the ICC, where a lot of the regulation is going to be removed, and I'm sure there are different views about what kind of oversight mechanisms should be left in place.

What can the Department—and what will the Department—do to encourage competition to protect the rights of these small shippers and to ensure that rural communities, especially the farmer elevators, many of which are farmer-owned co-ops, or small independent businesses, are going to have access to our transportation infrastructure?

To go on, so you can just answer all of it, can I assure my constituents, because people want to know what are we doing that practically can help them out, that you will work with Secretary Pena to monitor how this concentration in the transportation industry is going to affect agriculture, and also what specific mechanisms can you establish in the Department that Minnesotans can look to? I mean what office can we call? Who can we be in touch with? These are just a set of practical questions that I want to put to you.

Secretary GLICKMAN. Well, it's a good question. I raised this issue inside the Department a couple of months ago and we've put together a working group under Mr. Paul Kepler's leadership, who's seated behind me, to deal with the issue of rail car shortages, rate issues and problems, availability, so we're kind of like a central clearinghouse. Mr. Kepler is the person to contact where there are particular problems.

Quite frankly, the railroads have been very cooperative in talking to us about those problems as they occur. I have met with the American Association of Railroads, talking about this particular problem, and we've established kind of a liaison by which I can get to them concerns and complaints when there are shortages or rate problems that take place.

The ICC set up this Grain Car Council, as well. I don't know if you're familiar with it. One of the commissioners, J. S. Simmons over there, was very interested in that. They do have that now. USDA is involved with the Grain Car Council, which advises the ICC on grain car shortages and availabilities. As long as the ICC is still in existence, I think this is useful input for them, as well. So, those are two areas.

I also just want to let you know that also I'm very concerned about this issue because, as I said before, particularly at a time when we're seeing traditional farm program spending going down, and we're seeing a much more export market-oriented process at work, you must have access to the transportation, the railroads, to make that work.

So, you could see higher grain prices, which we have right now, but counterbalanced with much more significant problems in getting the cars to service or getting them at all.

So, we have to take a very active role in this and we have to be prodding the railroads all the time.

Senator WELLSTONE. So, you'll be working with Secretary Pena and others to monitor this?

Secretary GLICKMAN. That's correct.

Senator WELLSTONE. Let me just ask one other question. I keep thinking, with Kansas, was Mary Ellen—some of her opponents called her Mary "Yellin" Lease. Was she from Kansas?

Secretary GLICKMAN. She was.

Senator WELLSTONE. This goes back, Madam Chair, this goes back to the 1870's and 1880's, this whole issue of concentration of ownership.

Secretary GLICKMAN. Her line was "Let's raise a little more hell, a little less corn."

Senator WELLSTONE. Raise less corn and more hell, right. Not bad advice.

Mr. Secretary, I know that you've been concerned about the economic concentration in American agriculture—in grain trade, in livestock, as well. Can you make transportation part of your overall examination of concentration of ownership in the American economy, especially taking a look at how it affects small agribusinesses and farmers?

Secretary GLICKMAN. Well, as you know, we're establishing an advisory Committee on economic concentration in agriculture. It's largely geared to the livestock industry because that is within our bailiwick. To be honest with you, a lot of the transportation issues are within the bailiwick of the Justice Department or the Transportation Department.

But you can't look at all these issues without figuring out how a farmer or a grain elevator gets his or her crop into the marketplace. So, there will probably be some look-see in this area, but it's probably a little more in the other jurisdictions than ours.

Senator WELLSTONE. I would urge you to do so because I don't think you can really separate out these questions.

Well, Madam Chair, there are others. Thank you.

Chair MEYERS. Thank you, Senator Wellstone.

Mr. Brownback.

Mr. BROWNBACK. Thank you, Madam Chairman.

Welcome to the Committee, Secretary Glickman. You're looking fine.

Secretary GLICKMAN. So, are you, Sam.

Mr. BROWNBACK. It helps when we're winning in football, right? Sorry about that, Senator. I didn't mean to rub that in. It's been a touchy weekend.

A couple of questions that I had. I don't know if you have this at your fingertips but I'd appreciate your internal review group looking at these things.

I've been around this question for a little while, as well, when I was agriculture secretary in Kansas, and this has been a long-term issue for the agriculture industry, for the small shipper business for some period of time. I've wondered what the overall effect has been on grain prices of doing this because my sense of it has been actually that where you lose a railhead contact, you've got a loss in grain prices. I mean, you get a smaller differential because your cost of transportation goes up.

But sometimes some of the unit train effect has been in this business to actually improve prices in places, and I wonder what the overall effect has been actually on the agriculture industry.

Secretary GLICKMAN. We've done analysis of rates but not of grain prices. There is no question, as you say, that if you can move your grain in unit trains, you will get some benefits of lower rates and perhaps higher prices. But we have not looked at the issue of how it affects prices itself.

Mr. BROWNBACK. The other one I was curious about is we've had a lot of loss of grain elevators throughout the country, and I know particularly in Kansas. The small grain elevators had a great deal of difficulty.

How much has this contributed into that? Have you been able to quantify that if you have this loss of rail track and it's not picked up by a short line, we lose this percentage of grain elevators, then?

Secretary GLICKMAN. I don't have the numbers. Anecdotally I would say that there's been some loss of smaller elevators because of loss of track or abandonment, but there are experts here who know more about this than I do who'll be following me that you ought to ask that question.

Mr. BROWNBACK. Then do you have, by chance, anything on the percentages of grain shipped by truck or road versus railroad? I'm probably asking too particular a point.

Secretary GLICKMAN. It's overwhelmingly by rail. Fifty percent of grain is shipped by rail.

Mr. BROWNBACK. I appreciate your looking at it in the department and forming the internal task force because this has been a long-term problem. I'd particularly appreciate if they could consider some of these issues and, in the mode of what's going on in the rail industry, what can be done to help that small shipper and make those markets more accessible.

I don't know really what all there is, but to the extent you can come up with some of those things, I'd sure appreciate it.

Secretary GLICKMAN. Thank you.

Mr. BROWNBACK. Thank you.

Chair MEYERS. Mr. Luther.

Mr. LUTHER. Thank you, Madam Chair.

I certainly want to thank you for your testimony, Mr. Secretary. As I understand the way the ICC approaches these situations is that they do a balancing between the increased efficiencies, on the one hand, and the competition, the competitive effects on the other hand.

Does that basically mean that a merger can be approved even if the anti-competitive effects are very substantial?

Secretary GLICKMAN. I'm not equipped to answer it specifically except to tell you the tests are different than if the Justice Department would be viewing this from a question of market power, so to speak, and percentage of ownership. They consider economic compatibility and tests a lot more than the Justice Department would.

But the ICC has a very complicated formula for determining these issues that, as you know, will probably end. If it's terminated and abolished, those authorities will go to DOT or Justice in different degrees depending on the final outcome of the legislative process.

Mr. LUTHER. In your judgment, should more consideration be given to the anticompetitive effects?

Secretary GLICKMAN. I don't know about more, but I do believe that a focus on anticompetitive effects, not only in the railroad industry but on the shipping side of the industry, ought to be part of the equation.

Mr. LUTHER. Madam Chair, if I could, I know we're under call for a vote, but just to follow up on that, what studies are you aware of that do relate the rates, the rates charged to the competition? I mean, I think our general sense is that we would see some relationship, but what kind of actual, concrete studies have been done?

Secretary GLICKMAN. We have a 1989 study in USDA. That report concluded that competition among railroads has a statistically

significant fairly strong effect on rates, and we will get you a copy of that study.

Mr. LUTHER. Is that the McDonald——

Secretary GLICKMAN. That's a USDA study. There may be others, as well.

Mr. LUTHER. If I could, I'd appreciate that. Thank you.

Secretary GLICKMAN. Thank you.

Chair MEYERS. As you can hear, we have a vote in the House and so I think we will go to questions from Mr. Chabot and Mr. Bartlett and then go vote and come back as quickly as we can for our second panel.

Mr. Chabot.

Mr. CHABOT. Thank you, Madam Chair. In reference to the time, I'll be relatively brief.

Mr. Secretary, you mentioned the farm bill and, I think paraphrasing what you said, that you want to emphasize action which makes sense, business sense, when farmers are growing crops, rather than just to meet some sort of artificial requirement, either for subsidy or price support or whatever. We also want to emphasize and encourage exports, farm crop exports.

I just wanted to mention that we'd love to have the administration and yourself review and perhaps offer some input, maybe even support ultimately a bill which was sponsored by myself and cosponsored by Major Owens who, of course, is a Democrat from New York, which would especially eliminate all price supports, farm subsidies, basically no longer pay farmers not to grow crops 1 year after the legislation is passed and then signed into law.

So, we would love to hear your input. I know we don't have time here today to hear extended input but if you would like to comment on that, we'd love to hear it.

Secretary GLICKMAN. I would say it's rather unlikely that we would support that particular bill, but I do think that we're moving into an era of much greater planting flexibility and much greater orientation to the market. That's one of the reasons why transportation becomes even more important. As you try to give farmers the tools to market their crops and maybe not rely exclusively on very large grain companies, to do that, they need to be assured that those transportation systems are in place.

Mr. CHABOT. Just to follow up, even if we're not ultimately successful in passing the bill, I would like to take the discussion in that direction, that we can at least phase out subsidies and price supports as quickly as we possibly can because I think everyone would benefit if we could do that, both the consumer and farmers, as well. Thank you very much.

Secretary GLICKMAN. Thank you.

Chairman BOND. Mr. Bartlett.

Mr. BARTLETT. Thank you very much. Since we have a vote call, I'll be brief.

I have two quick questions. One is in the communications industry, one entity owns the lines and anyone can use them, so that we're now moving to more and more competition, which has done what competition always does—it brings down the cost and it improves quality of service.

To what extent is this the practice in the rail industry?

Secretary GLICKMAN. Well, as part of the mergers in the past, there's been some requirements that railroads let other short-line and other carriers use their lines. To have competition that works, you have to have other players in there, and as opposed to communications—I don't know that much about the legislation but I do know that there's a great deal of an abundance of producers of product and transporters of the actual message.

In railroads you've got this physical line that's out there. It's a hard piece of capital equipment that's owned by the railroad who operates on it.

Mr. BARTLETT. Communication lines are the same thing.

Secretary GLICKMAN. You have not seen a large number of competitors spring up to use those lines because of the enormous capital costs associated with operating railroads. Now, you've had some minor success, and minor is a relative term in terms of numbers of trackage in some of these abandonment cases, but significantly, most of the rail traffic in America is done through large volume trafficking, unit trains, that kind of thing, where it's very hard for new players to get into the act.

Mr. BARTLETT. But we don't have two parallel lines for communication. Anybody can use a common line. Why can't that be true in the rail industry and why can't we have competition across the country, no matter who owns the line?

Secretary GLICKMAN. I think in theory you could but in practice, if you're located 250 miles southeast of Kansas City, in the middle of an extremely underserved area, somebody has to build the lines there because the railroads aren't generally operating lines in underserved areas.

Most of rural America is in underserved areas where there are not lines.

Mr. BARTLETT. You're talking about new lines.

Secretary GLICKMAN. That's right.

Mr. BARTLETT. I was talking about the existing lines and competition there.

Secretary GLICKMAN. A lot of those lines have been abandoned. I'm not an expert on the availability of trackage but I don't think this is exactly like the communications industry where you can pick up a cellular phone and tap into a system, no matter where you are, without much capital expenditure. In the case of railroads, it's very expensive to get into this business, enormously, with small volumes of trafficking. That's the thing.

Now, some of the short lines have had some success, but I don't know if you can parallel that reasoning into saying that there's all that much competition in the industry.

Mr. BARTLETT. I just thought that there might be parallelisms where clearly in communications they have a number of companies which are offering service and they all use common lines; they certainly need to pay their fair share.

Just one last quick question. In Maryland we're a net consumer of grain. Generally our grain here costs about 25 cents more than the Midwest, which represents the cost of shipment.

At what level does trucking become competitive with railroads, so that we have competition there?

Secretary GLICKMAN. Not in long distance trafficking. It takes so many times more trucks in order to get an equal amount of grain on there.

So, shorter distance, you see a lot of grain moved by trucks but not long distance. It's just very uneconomical.

Mr. BARTLETT. Thank you very much.

Chairman BOND. Thank you very much, Mr. Bartlett.

Senator Bumpers, do you have any additional questions?

Senator BUMPERS. I'd like to put a couple of statistics on the record regarding the question I asked you earlier, Mr. Secretary. It comes from a book that's called "Railroad Facts, 1990 Edition," put out by the Association of American Railroads. I think just these statistics might help us a little bit.

In regard to the chair's original statement about the reduction of Class I railroads, I think it's important to note that a Class I railroad, by definition, is one whose revenues exceed $255 million a year. So, this really regards them.

First of all, there has been a reduction, with the Burlington–Santa Fe merger, we now have 10 Class I railroads out of 18, I believe, as recently as 7 years ago, maybe 8 years ago.

So, what you have is 2 percent of the railroads of the country are Class I railroads, 2 percent. They have 73 percent of the mileage, 89 percent of the employees, and 90 percent of freight revenues.

Having said that, those figures don't mean an awful lot unless you can document, with those figures, that competition has been eliminated and that other railroads or even maybe some Class I railroads have been hurt by these mergers.

As everybody knows, in the 1960's and 1970's we had a lot of railroad bankruptcies in this country. We had to provide a lot of relief to keep some of them going.

So, having done that, one of my concerns is I want to make sure we don't go back to the reasons for the Interstate Commerce Commission to begin with, back in 1887, when we felt we had to regulate monopolistic tendencies.

I just wanted to put those statistics in the record, for whatever they're worth. We need to follow that up, as I say, to determine whether or not there's been any elimination of competition and how it's occurred and so on.

Secretary GLICKMAN. Senator, I will tell you that is one of the issues that our working group is looking at right now.

Senator BUMPERS. One other observation on that. We had a situation like this in my State, that these railroads don't have the cars. You pointed this out, and of course it's very difficult for them to take the massive increase in demand during the harvesting system, when they don't really need that many cars the rest of the year. So, I'm sympathetic to the railroads from that standpoint.

But we had the situation in our State where they couldn't supply the cars in the rice country during rice harvest. The result was a shipper such as Riceland Foods, which, of course, is the giant rice cooperative in my State, began to look for alternative methods of shipping, and they have not gone back to the railroads. They still do 35 to 40 percent of their shipping by railroad but they used to do a lot more. Because they couldn't get the cars when they had to have them, they started searching for alternative methods of

shipment. They've been reluctant to go back to the railroads, not knowing whether those cars would be available in the future or not.

Thank you, Mr. Chairman.

Secretary GLICKMAN. I just might say it's a very good point. Some people, and this is an important point for us to consider, say that you can't consider competition in railroads alone; you must consider the competition in trucking and other means of transportation. I think there's some truth to that but again, when it comes to moving grain great distances, and it may be true with rice, as well but I don't know for sure, but in the grain area it's very difficult on some agricultural commodities for long distance shipments using trucks.

Senator BUMPERS. Well, let's face it. Sometimes there aren't alternatives. There simply are no alternatives available.

Chairman BOND. Thank you very much, Senator.

One final thing, Mr. Secretary. You mentioned the shortage of rail cars in the Midwest. Do you have any comments on how car ordering systems can affect small businesses such as grain elevators?

Secretary GLICKMAN. Clearly there is the potential for prejudice against lower volume users. Again, it's one of the things that we're looking at. Frankly, railroads make more money off of higher volume users. It's a natural phenomenon and order of things. It's not an evil practice.

One of the things we have to figure out is in a deregulatory environment, which I think in some sense there is general consensus on, although I think in some areas it's gone too far, how you protect the smaller shipper in the process of ordering cars, particularly when you're involved in moving grain through large unit trains and other means that are more profitable.

Frankly, this is something we need to keep a dialogue with the railroad industry on. I have found that through keeping the communication lines open and letting them know our concerns and complaints, we can work through some of these things.

Chairman BOND. Well, Mr. Secretary, thank you very much. I know you have many items on your plate. We appreciate your time. We look forward to continuing to work with you and again, we're grateful for your testimony.

With that, I am going to ask that our witnesses come forward. We will get everybody lined up and wait till the chair returns and the Members of the House. We have a very distinguished and large panel.

Mr. Phil Hoffman, who manages Hoffman & Reed, an elevator and farm supply firm located in Trenton, Missouri; Mr. James Jundzilo, the transportation manager for Tetra Chemicals in Woodlands, Texas; Mr. Butch Fischer, president of Scoular Grain, a diversified agribusiness headquartered in Omaha, Nebraska; Mr. William York, manager for the Lange Company, an independent grain elevator in Conway Springs, Kansas; Mr. Ned Leonard, manager of communications and Government affairs at the Western Fuels Association in Lakewood, Colorado; Mr. Ed Emmett, president of the National Industrial Transportation League, a trade association of shippers based in Arlington, Virginia; Mr. Richard Bar-

ber, transportation economist based in Bethesda, Maryland; and Dr. Curtis Grimm, professor at the College of Business and Management, the University of Maryland in College Park, Maryland.

Gentlemen, we're delighted to have you. Won't you have a seat.

Now that I have your attention and I have a moment, I have been asked by Senator Pressler, who also has responsibility in this area, to present his statement for the record, and hearing no objections, I will insert the statement.

As Senator Pressler says, "As a Senator from South Dakota, whose economy is based primarily on agriculture and small business, and as chairman of the Senate Committee on Commerce, Science and Transportation, the impact of mergers on small shippers obviously is of great concern to me. The trend toward increased concentration of the largest railroads heightens this concern.

"However, Class I concentration is not the only dynamic within the industry. As the Class I's continue to get bigger and bigger and fewer in numbers, department of smaller, short-line and regional railroads increases. To a large extent, the concerns of small shippers often mirror those of the small railroads. Together they both are often dependent on a single Class I for car supply, market access, switching rights and other fundamental matters.

"All parties in discussion over these kinds of issues have legitimate concerns. These concerns need to be better defined in order to resolve them on a permanent basis in this rapidly changing industry. I think it is entirely possible for the industry to resolve these issues and encourage that process.

"Done correctly, it could provide more effective relief to legitimate small shipper concerns and be far less problematic for Class I's than any Government-imposed sanctions.

"There should be no doubt the Commerce Committee perceives the small shipper concerns as very real. There is a definite problem. It must be addressed. We have made that point emphatically clear in the Interstate Commerce Commission sunset legislation. Indeed, the bill, as introduced, provides a mechanism for resolving these kinds of issues.

"If the industry does not choose to employ the opportunity in a constructive manner, those resisting reasonable efforts to address legitimate concerns through industry compromise are likely to face a far less favorable outcome in the form of a Government solution.

"Finally, I emphasize that in my view, the primary problem is for the small business, both shippers and railroads. Throughout the ICC sunset legislation process and continuing today in other forums, it seems to me other interests are quick to use small business as a means to achieve their agenda. I intend to remain vigilant to ensure operators are not used as fronts for someone else's agenda. I encourage the same vigilance for others attempting to explore these legitimate concerns of the small shippers."

That is the end of the statement by Senator Pressler, who is the chair of the Commerce Committee.

We won't declare a formal recess but invite everybody to relax and enjoy the beautiful surroundings we have here.

Chair MEYERS. I thank Senator Bond for getting everything organized here. We have a number of witnesses and so while we will

light the lights and ask you to observe them, but when the light turns red, don't feel like you have to break off in a middle of a sentence. If you could conclude your remarks as soon as possible thereafter, it will give us some time for questions.

Our first witness is Mr. Phil Hoffman and Mr. Hoffman manages Hoffman & Reed, an elevator and farm supply firm located in Trenton, Missouri. I believe that Mr. Hoffman is a constituent of Senator Bond and Senator Bond, if you would like to add any remarks here?

Chairman BOND. Madam Chair, I've already given these gentlemen an introduction, probably butchered a few names in the process. We're delighted to see all the witnesses and we'd welcome them to correct my pronunciation if I have missed it previously. Phil?

TESTIMONY OF PHIL HOFFMAN, SECRETARY, HOFFMAN & REED, TRENTON, MISSOURI

Mr. HOFFMAN. Thank you, Madam Chair. I'm not sure how this works. Frank complains and I get sent to Washington.

As the Senator stated, I am Phil Hoffman. I'm representing Hoffman & Reed, Inc., a firm that my brother and I manage. It's a family owned country elevator, a small country elevator and farm supply firm handling grain, feed, seed, fertilizer and crop protection inputs. We have about 33 employees and we're located in Trenton, Missouri. It's a town of about 6,500 in north Missouri. We're located on what used to be the spine line of the Rock Island Railroad running from Minneapolis to Kansas City.

The business was started in 1949 by my uncle Frank and my father, both of whom are still active. They began selling sacked feed, buying cream and eggs from local farmers. In 1952 they started direct loading of rail cars. They loaded 55 boxcars that first year. The railroads told us we needed to spread out our shipping season so we started expanding the elevator. Today we have a storage capacity of 1,900,000 bushels in two locations and we have the ability to load about 12 to 15 hopper cars a day, which definitely keeps us in that small shipper class.

In the 1960's the Union Pacific petitioned the ICC to purchase the Rock Island. After some 12 years of deliberation, the proposed sale was denied by the ICC. So, we've seen the ICC from both perspectives.

In March 1980 the Rock Island filed bankruptcy. Following a couple of years of directed service by the KCT, the Chicago Northwestern purchased the remaining tracks of the Rock Island. The CNW invested in the line, brought train speed up to about 50 miles an hour from the 5 to 10 miles per hour that the Rock Island was operating under following all the years of neglect. For the past 12 years we've enjoyed a good relationship and much improved service with the CNW.

This past spring, the Union Pacific acquired the CNW and the two systems merged operationally in October, this fall. Over the past 6 years we have loaded an average of 350 to 400 hoppers a year, consisting of four different commodities: Corn, soybeans, wheat and milo. We also receive 35 to 40 cars of fertilizer a year.

In 1995 we've loaded 208 cars. Since our fall harvest began, which also coincided with the merger operationally of the UP and the CNW we've loaded—in my written testimony I said five. We received one car yesterday, so we'll have to make that six. That's at a time that is normally our peak shipping season.

We came into fall expecting difficulties with rail service. We knew that cars were tight and we expected the transition from the CNW to the UP would not be smooth. That was the one silver lining of having a small crop this year. We were able to handle the harvest without rail cars. But our concern is more for the future than what happened this fall.

From our conversations with the CNW and the UP and processors and elevators that receive our grain, we've been given little encouragement for improvement anytime soon, if at all. All indications that we get are that the UP is committed to a program of shuttling large unit trains of 75 to 100 cars between large shippers and large users. The potential benefits of the UP we saw for Hoffman & Reed and our farmer customers, in terms of expanded markets through the UP system, will mean little if we don't receive hopper cars to load.

We understand and fully expected change with this merger. We also understand growth and the efficiencies the megarailroads are attempting to accomplish. However, if megarailroads are unable or unwilling to provide service to small shippers, then opportunities need to be devised for others who are willing to provide that service. We, as a small shipper, need more than a wave from the megarailroads as they speed down their track to efficiency.

I thank you for the opportunity to tell our story.

Chair MEYERS. Thank you very much for being here, Mr. Hoffman.

Mr. Jundzilo. Is that close enough? Jundzilo.

TESTIMONY OF JAMES F. JUNDZILO, TRANSPORTATION MANAGER, TETRA CHEMICAL COMPANY, THE WOODLANDS, TEXAS

Mr. JUNDZILO. It's real good. It's exactly correct.

Mr. Chairman, Madam Chair, I'm kind of nervous, so if I stutter—my name is Jim Jundzilo. I am a transportation manager at Tetra Chemical. I have 30 years experience in transportation and distribution, including academic consultant and operations management. I have an MBA from Youngstown State University. I'm an ICC practitioner and a certified member of the Society of Transportation and Logistics.

I am responsible for rail negotiation and rail service strategy for Tetra Chemicals. Tetra Chemicals is a rail service consumer. The service required is North America. Tetra Chemical utilizes all major Class I railroads. Volume impact to the Class I railroad is marginal. Tetra Chemical has less than 800 rail car movements annually. Thus, in most cases, railroad consolidation and mergers have a negative impact on Tetra Chemical.

I have submitted a written statement which I would appreciate being included in the record. I would like to amplify on my written statement and make the following three points.

The first point: I currently benefit from the Union Pacific and Southern Pacific competition and my ability to compete in the marketplace would be dramatically impaired if these two companies merge.

Second, the proposed merger between the UP–SP will prevent my company from selecting a railroad of my choice and one in which I have confidence. Based on what I know at this time, if this merger is approved, my business would be served only by one railroad for long-haul transportation. When nearly 50 percent of my costs is transportation—I want to emphasize—50 percent of my product cost is transportation, the thought of being at the mercy of one railroad is scary. This merger can clearly threaten my company's ability to compete.

Third, my experience with the railroad mergers have been highly unfavorable. I urge you to encourage Congress to address this problem of merger standards. This proposed merger should be governed by antitrust standards, not the current ICC standards. The ICC standards address public interest and necessity, and not necessarily competition. If the ICC standards of public interest are applied, this merger may be approved and the public will suffer.

Let me address for you issues of competitive access and captive shippers. First, competitive access. Our Lake Charles, Louisiana plant has access to three railroads: The Union Pacific, the Southern Pacific and Kansas City Southern. The Union Pacific uses a switching carrier to service our plant.

The issue with competitive access is limited by the destination carrier. Thus, if Southern Pacific or Union Pacific delivers, Kansas City Southern would be discouraged from participation in the joint routes. Only on paper does it appear that we have competitive access when, in fact, we are restricted to any Western State rail business to be routed on the Union Pacific or Southern Pacific lines. We cannot utilize the Kansas City Southern lines because the Kansas City Southern Railroad is regulated to a regional base carrier.

Now, consider the position of a captive shipper who has access to only one railroad. Tetra Chemical has two plants that would be considered captive shippers: Washington, West Virginia and Norco, Louisiana. Both plants have water barge access. If I were to ship on waterways, competitive conditions would normally exist. Heaven help me if I have to go inland.

Captive shipping hurts most if only one railroad controls destination because of route restrictions. I'd like to make this point: Competitive access can be just as captive as a single rail service. If Union Pacific and Southern Pacific merge, I would only have one railroad to go West because of route limitations. The Lake Charles, Louisiana and Norco, Louisiana plants would be directly affected by this limitation. I feel this would have a negative impact on Tetra Chemical because of lack of competition in the service area.

In conclusion, I have no problem with deregulation. However, if deregulation occurs, it is important that it occur with proper antitrust oversight. We cannot permit further deregulation when the current Government standards allow megamergers and concentration in the marketplace with very little consideration of competition.

This is what is happening under ICC standards. When the country is confronting the largest single railroad merger in its history and faced with unparalleled railroad concentration, this merger must be stopped until a very careful evaluation of merger standards has been completed. I am very worried that shippers don't even know what the rules will be under the new agency replacing the ICC.

Deregulation can only work as long as competition is maintained. I strongly recommend that the current standards or mergers in the railroad industry be changed. We must put more focus on competition, involve the antitrust laws, and competition in the public interest will then be maintained and protected. Thank you.

[Mr. Jundzilo's statement may be found in the appendix.]

Chair MEYERS. Thank you very much, Mr. Jundzilo.

Mr. Fischer is the president of Scoular Grain, a diversified agribusiness headquartered in Omaha, Nebraska.

TESTIMONY OF DUANE "BUTCH" FISCHER, PRESIDENT, SCOULAR GRAIN COMPANY, OMAHA, NEBRASKA

Mr. FISCHER. Good afternoon, Chairman Bond and Chair Meyers and members of the Committees. Thank you for giving me this opportunity today. My name is Butch Fischer. I'm president of the Scoular Companies, which is a diversified agribusiness concern headquartered in Omaha. We also have 40 employees in Overland Park, Kansas, which I understand is in your district.

I've been with the Scoular Company for 23 years and primarily in grain merchandising positions until becoming the president in 1990. I especially appreciate Secretary Glickman's concern for country elevators and I plan to respond to his request for suggestions on how to improve agricultural competitiveness.

The Scoular Company actively trades grain and grain by-products throughout North America. We physically handle about 65 million bushels of grain through our facilities in Missouri, Montana, Kansas, and Nebraska, and we trade an additional 300 million bushels.

Our 14 grain shipping facilities are located throughout the West and all but two are rail-served. Union Pacific, Burlington Northern and several short lines serve these facilities. In fact, Mr. Bond, we just built a facility in Harrisonville, Missouri on a short line this year.

We also own or lease 557 rail cars and we pay over $65 million a year in freight, which $13.5 million of is truck freight.

I'm well acquainted with railroads and their role in businesses like mine, which is one that deals in bulk commodities and depends on efficient rail service. Ours is not a small business but we do merchandise the produce and output from small businesses which are basically family farms.

I have observed consolidation in the rail industry firsthand over the past two decades as the number of Class I railroads has declined. The remaining railroads today are more efficient, more productive, and better able to serve grain shippers, large and small, than they were 15 years ago.

We have increased market outlets for our grain and the larger railroads resulting from these mergers are also capable of making more resources available to move grain.

Without the rail mergers of the past two decades, the transportation infrastructure would be in even worse condition than I think it is today. Consolidations have created opportunities for producers and merchandisers to find new markets for their products.

None of the recent mergers have reduced competition for any of our facilities, and I fear greatly that if the Union Pacific–SP merger were held up, our situation would deteriorate significantly. There was reasonable balance in the Western United States when we had four carriers, the weakest of which was and remains the Southern Pacific. A merged BN–Santa Fe, which is a done deal and the merger is complete, has the clout and the power to take the Southern Pacific out of business, and I think it would have a disastrous impact on our business and many others.

This hearing focuses on the effect of rail mergers on small businesses, and frankly I don't think that rail mergers have a large impact on competition. If we're looking for a big bogey man here for the problem, I think Congress should look at itself.

I'd like to go through a little saga here of our industry and what's happened in the last 25 years. The 1970's saw unprecedented prosperity and growth in agriculture. Ninety percent of the covered hopper barges that haul grain in this country today were built prior to 1980.

In 1980 my company operated 70 facilities. As I said, we now operate 14. We had 550 employees and today we have 150. In 1979 we purchased 300 rail cars at a cost of about $14 million and within 1 year President Carter embargoed our grain exports to the Soviet Union and especially damaged agriculture to the extent it hasn't recovered from since.

In 1983 the Government instituted the payment-in-kind program, which was the largest acreage-idling program in history. The 1985 Farm Bill put in place annual acreage reduction programs and set in place the conservation reserve program, which idled 36 million acres of farmland for the last 10 years, all of which is still out of production, and an additional 650,000 acres was just added in the last 30 days.

The 1990 Farm Bill was a continuation of the '85 bill and we basically have been struggling along ever since then.

The transportation infrastructure to haul grain was devastated by the impact of reduced production and reduced exports. In 1994 we saw a 60 percent increase in corn export demand from this country and we do not have the infrastructure in place to satisfy that demand.

When we're talking about a rail car shortage, don't forget to look at barge supplies. They're actually in worse condition than the railroad industry and have made the rail industry look worse, in fact, than it actually is. When you talk about a grain car shortage in Iowa or Minnesota, that's as much a barge shortage as it is a rail car shortage.

I know I have the light on here. In conclusion, I'd like to say what the U.S. really needs to do is expand grain production permanently. The capital to come in and improve our infrastructure will

happen, but it's not going to come in quickly. I just went through the saga. It only takes one of those things to turn our whole industry upside down.

As recently as 1990, my company lost $1 million on our own rail cars. Now I'm very glad I have them but it wasn't that long ago that I was very sorry I had them, and we remember those situations.

If we were to increase production on a permanent basis, some of those 56 elevators of mine that were sold or closed, one of which is in Kansas City, which is closed right now, would be reopened. Jobs would be created; rural economic development would accelerate.

I really would suggest that Congress resist the temptation to get more involved in these kinds of issues and instead, go the other direction. Just get out. Thank you.

[Mr. Fischer's statement may be found in the appendix.]

Chairman BOND. Thank you very much, Mr. Fischer.

Now we turn next to Mr. William York, manager of the Lange Company in Conway Springs, Kansas.

TESTIMONY OF WILLIAM F. YORK, MANAGER, LANGE COMPANY, LLC, CONWAY SPRINGS, KANSAS

Mr. YORK. Thank you, Madam Chairman, Mr. Chairman. I want to thank you for the opportunity to appear here before you today. I've submitted a written statement which I would appreciate being made a part of the record.

Chairman BOND. Without objection, it'll be made a part of the record.

Mr. YORK. I want to express my appreciation for the Secretary of Agriculture appearing before you also. He's a long-time friend and good friend of mine and our industry.

I would like to amplify a few points in my written statement, with your permission, and some of the points I want to raise is first, the proposed UP–SP merger will hurt competition in my area of the country. Second, we must have more service available than the UP–SP merger to broaden our marketing opportunities. Third, there are a multitude of small businessmen and women in my area of the country who will suffer if this merger goes through as proposed.

Again, my name is Bill York, manager of Lange Company LLC in Conway Springs, Kansas, which is about 30 miles Southwest of Wichita. We're a small community in south central Kansas, a receiver of grain, primarily wheat, and we ship to a myriad of grain terminals and brokers.

We're dependent on truck and rail transportation in our area to move products to market. We'd rather move it by rail because we can get our money faster by rail than you can by truck. It costs us less interest. Part of our problem is the rail rate is much higher than the truck rates from our elevator.

Furthermore, for many, if not all of our grain movements, to out of State locations, trucks are not an effective competitor and we find ourselves with no alternative but to ship by rail. For example, in south central Kansas, this locks our shippers into shipping only

to the Gulf and that really restricts—they're not the only market, a lot of times.

Our rates continue to increase, not decrease. These high rail rates are seriously eroding our ability to compete. Our concern is that the proposed merger of the larger railroads will create a duopoly in our area, meaning two large carriers completely dominating rail transportation in the Western United States and therefore creating a noncompetitive environment for shippers to operate in.

As mergers continue to happen, as has been pointed out several times today, our options get less and less. We're therefore stressing the need for additional Class I's in our area to keep rates competitive and allow the possibility of more competitive rates and to provide equipment alternatives.

We have been told by various short-line railroads that, if allowed, they could offer rates that would be competitive to truck rates, but unfortunately, most of the short lines connect with only one large Class I carrier and thus serve as feeder carriers. Even if there is a short line that connects with two carriers, for example, the UP–SP, as those carriers merge, these short lines and the shippers located on these short lines lose the ability to benefit from the UP–SP competition.

We need the Small Business Committee and Congress to support our small business and our country rail shippers in their attempt to remain in business and continue to be a part of small town U.S.A. The best way they can do that is by expressing their concern over these rail megamergers.

Having been a part of this grain industry for 32 years, I've seen disruptive service resulting from consolidation of railroads into megaconglomerates and the competitive short line may no longer be present.

For example, we understand the UP has informed some Iowa customers of rail service dislocation resulting from the UP–CNW merger. I'm not really a lawyer or an economist but if the UP–SP are allowed to merge, thus reducing the number of railroads in the West from four to two in less than a year and a half, perhaps there's something wrong with the merger standards. We're not able to reduce our transportation costs, which creates an atmosphere of business failure.

At the close, I would like to leave you with an example with the previous merger on a Class I. A key employee of that Class I, which is a done deal, a key employee told me personally that they were not interested in the small shippers, such as myself, or providing service to us.

My recommendations are, number one, for purposes of filing rate complaints, one must maintain a Government agency similar to the ICC.

Second, is to allow railroads to arrange reciprocal switching, therefore giving us additional routes to move grain.

Third, to encourage the UP–SP to allow the KCS railway to replace the SP rights gained in the BN–Santa Fe merger proceeding to serve Kansas grain shippers.

Fourth, is to revise the current merger standards to focus more on the loss of competition under existing law and less upon so-

called efficiency gains or allow the Department of Justice to review rail mergers as they do for other business, including airlines.

Thank you for your attention.

Chairman BOND. Thank you very much, Mr. York.

Before turning to Mr. Leonard, I must apologize to our witnesses. You've heard of Murphy's Law. Well, when it comes to scheduling hearings and votes in the House and the Senate, Murphy was an optimist. I'm getting communications; Senator Bumpers and I have a vote at 3:30. We have some other commitments.

I will submit questions for the record. I hope to be able to hear the rest of the testimony but again, I apologize. That's the way it works around here. My colleagues will be, as well, reading your testimony and probably submitting questions for the record.

Now I'd like to introduce Mr. Ned Leonard, manager of communications and Government affairs for the Western Fuel Association in Lakewood, Colorado.

TESTIMONY OF NED LEONARD, MANAGER, COMMUNICATIONS AND GOVERNMENT AFFAIRS, WESTERN FUELS ASSOCIATION, INC., LAKEWOOD, COLORADO

Mr. LEONARD. I very much appreciate the invitation to appear today. My general manager and chief executive officer Fred Palmer's travel schedule would not enable him to be here to testify but he did work out detailed testimony and I hope, with your permission, that it can be reprinted as part of this record.

Chair MEYERS. Without objection.

Mr. LEONARD. Thank you. It was a pleasure to hear the Secretary of Agriculture this afternoon. Secretary Glickman was one of the captive shippers' earliest allies in Congress. As an original cosponsor of both the Railroad Anti-Monopoly Act and the Clayton Act amendments, Mr. Glickman led a bipartisan coalition of diverse groups in tackling this problem, years ago. It's a problem that is rendered all the more acute by recent changes, both within the structure of the railroad industry and within the structure intended to regulate and govern that industry.

What is at issue are the efficiency of free markets, fairness in interstate commerce, and fundamental principles of antitrust law.

As a producer, purchaser and shipper of 23 million tons of coal for 12 consumer-owned electric utility power plants throughout the Great Plains, Rocky Mountain, Southwest States and in Louisiana, and as the largest single purchaser of coal from the Powder River Basin in Wyoming and Montana, Western Fuels Association, its member utilities, the coal industry and the electric utility industry are partners with the Nation's railroads in an enterprise that is central to our economy's continued vitality. That enterprise is supplying electricity.

But there's a sticking point in the relationship. Those shippers who have the means of securing competitive bids among railroads are paying less and less. Those of us who are captive shippers are paying more and more. For shippers who are captive to a particular railroad, there is no enjoyment of the benefits of free markets and competition. This point can be no better illustrated than it is by an exchange of correspondence between Western Fuels and the Burlington Northern–Santa Fe.

By way of background, Western Fuels applied to the Interstate Commerce Commission for trackage rights as a condition of the Commission's approval of the merger between the Burlington Northern and the Atchison Topeka & Santa Fe railroads. We were not alone in making such a request, but we were singular in our proven record of successful operation of two railways. Our motivation was the potential to create competition between the Union Pacific and the BN.

At present, one of our members, Sunflower Electric Power Corporation, a cooperative in Western Kansas, pays millions of dollars per year in above-market costs for coal deliveries at its Holcomb station, absent competition. Our concern is BN's ability to monopolize the entire coal haul, once merged with the ATSF, thereby effectively constraining competition with the UP for the traffic. The continued economic viability of Sunflower's investment in its power plant is at stake.

The ICC denied our trackage rights request. We've appealed that decision. But, nonetheless, on September 25, Western Fuels sent two letters to BN's coal business unit. In one, we reiterated our request for negotiation of trackage rights to Holcomb. We pointed toward BN's voluntary grant of trackage rights to Southern Pacific and stated our belief that by this action, BN is obliged to voluntarily deal with Western Fuels under similar terms and conditions. It is our view that under applicable Federal law, BN cannot discriminate among railroad competitors for the purpose of maintaining a monopoly position.

Our second letter requested trackage rights along the joint line in the Powder River Basin where both the UP and BN already operate, but where real competition is constrained by a territorial restriction agreement.

Our letters were clear. We would negotiate with the BN to establish a fair value for trackage rights, taking into account BN's substantial investment in track and various improvements it has made. Nonetheless, BN–SF's response was abrupt and back of the hand.

The full text of the letters is submitted for the record, but let me quote the relevant paragraph in BN–SF's response. It is, in effect, Exhibit A in the case of captive shippers in their dealings with increasingly monopolistic railroads.

BN–SF wrote, "We're not interested in granting trackage rights to any carrier over the routes you describe in your letters. Your view that voluntarily granting trackage rights over other rail lines to other common carriers obligates us to grant trackage rights to any specific party over any specific part of our railroad is a novel idea, but certainly not supported by any regulatory requirement of which we are aware."

We submit that this situation cries out for the sorts of antitrust regulation to which both the electric utility and the telecommunications industries are subjected. For too long, railroads have been able to hide behind a feeble vestige of regulation in the Interstate Commerce Commission, using the Keogh doctrine as protection from fundamental anti-trust law.

We would urge that Congress seriously consider those portions of Canadian transportation law affecting competition among carriers.

Or you might consider amending the Clayton Act. Other remedies no doubt can be devised.

In any case, in the face of increased merger and acquisition activity among railroads, it's important that Congress pay close attention to the potential for anticompetitive activity and to the need for competitive access to essential facilities.

We commend you for your early and your timely attention to this need. Thank you.

[Mr. Palmer's statement may be found in the appendix.]

Chair MEYERS. Thank you, Mr. Leonard.

Our next witness is Mr. Ed Emmett. Mr. Emmett is the president of the National Industrial Transportation League, a trade association of shippers based in Arlington, Virginia. Mr. Emmett.

TESTIMONY OF ED EMMETT, PRESIDENT, NATIONAL INDUSTRIAL TRANSPORTATION LEAGUE, ARLINGTON, VIRGINIA

Mr. EMMETT. Thank you, Madam Chair. We do appreciate the opportunity for this timely hearing.

The National Industrial Transportation League is the Nation's oldest and largest shippers organization. We represent shippers of all sizes, of all commodities, using all modes of transportation. the league was formed in 1907 specifically to deal with the Interstate Commerce Commission and with rail regulations at the Commission.

the league strongly favors deregulation. the league, being shippers and users of transportation, strongly favors an efficient rail industry. But we're here today to make sure that everyone understands that there's a fundamental difference between railroads and other modes of transportation.

In a deregulated environment, if any shipper at a particular facility does not like the service provided by, say, a motor carrier, they call another motor carrier. If they don't like their air cargo carrier, they use another air cargo carrier.

However, if you're served by only one railroad, you cannot call another railroad to come to your facility. It just doesn't work that way. Therefore, the rail system has to be treated in a somewhat different manner in a deregulated world.

Now, against this background, I would like to address briefly the issue of rail mergers. My written testimony, I forgot to say at the beginning, I hope you'll have submitted for the record.

Chair MEYERS. Without objection, all of the testimony will be submitted for the record.

Mr. EMMETT. I came to town in 1989 as a member of the Interstate Commerce Commission. I was appointed by President Bush and served until 1992. During that entire time, there has been an undercurrent regarding rail mergers.

The statistics, which have been stated over and over about 42 Class I railroads in 1980, 10 Class I railroads today, soon to be 9, possibly 8, has always raised a question in people's mind about how few are too few? At what point should we shift and talk about competition, because the standards that are applied by the ICC, as other witnesses have testified here today, are applied with 1980 in mind, those days when the railroads were in dire trouble, when

there was a need to maintain an efficient, effective rail system. What could we do to keep those railroads in business?

The world has changed dramatically since 1980. We're no longer in that situation. We're now, League members believe, in the position where competition needs to be considered much more strongly.

Our first choice is to have rail mergers considered by the Department of Justice, just as mergers in every other industry are considered. There's nothing particularly unique about the railroad industry today that would say it needs to have its own agency to consider mergers, particularly since Congress is now looking at sunsetting or eliminating the Interstate Commerce Commission.

We've all recited the number. There are only 10 Class I's. Why would we set up a new special agency in the Department of Transportation to handle the few mergers that might remain? Why not go ahead and give those mergers to the Department of Justice, where they already have the expertise in dealing with mergers and could apply competition standards?

If Congress, though, decides to transfer merger jurisdiction to a newly created board or panel within DOT, then we have four specific suggestions that I would like to leave you with today.

First, require that railroads compete with one another and not just with other modes of transportation. There are many, many shippers that can't use other modes of transportation. There is a Canadian system, which has been referred to. There are reciprocal switching arrangements that can be regulated and put into place. But there has to be rail-to-rail competition.

Second, change the rail merger review process, no matter who does it, to focus on the anticompetitive aspects of a merger, and provide the Department of Justice a more direct role in the process, even if you don't give them the ultimate jurisdiction.

Third, require that any agreements between railroads regarding trackage rights, overhead rights and haulage agreements be made part of the public record and part of the approval process.

Finally, number four, require any proposed yet unfilled mergers to be put on hold until we know what agency is going to decide those mergers and under what standards. It's unrealistic to expect shippers and other interested parties to be spending the hundreds of thousands of dollars necessary to analyze a prospective merger when we don't even know what rules and standards are going to apply.

I thank you for the opportunity and look forward to working with both Committees and for your questions later on.

[Mr. Emmett's statement may be found in the appendix.]

Chair MEYERS. Thank you very much, Mr. Emmett.

Our next witness is Mr. Richard Barber, and Mr. Barber is a transport economist based in Bethesda, Maryland.

TESTIMONY OF RICHARD J. BARBER, BARBER & ASSOCIATES, BETHESDA, MARYLAND

Mr. BARBER. Thank you, Mr. Chairman and members of the Committee.

There seems to have been a bit of a current of discussions going on here that suggest that there's something automatically inconsistent between competition and mergers, rail mergers specifically.

In fact, there isn't. Rail mergers, including the proposed Union Pacific–Southern Pacific application, can build and create much more intense competition and provide shippers of all sizes with much better service. That ends up spelling more competition, not less.

There seems to be also some hint that you can get someplace in appraising competition by looking at or thinking in terms of numbers. Of course, if any two firms in any industry merge there's one less. That doesn't mean anything in terms of service to customers, whether they be big companies or small companies. I say that from the perspective of someone, like myself, who has consulted to the House Small Business Committee, to the Senate Small Business Committee, and who has served, as I have, on the staff of the Anti-Trust Subcommittee of the Senate. I strongly believe in competition, but competition is not measured solely by numbers.

Let me take an example in the real world. In the State of Washington today and in the Pacific Northwest generally there are a large number of small lumber mills. Most of those, almost all of them, are served by one railroad. Some of them are served by BN–Santa Fe, which, as a result of its recent merger, will have efficient single line service throughout the Western United States. They can ship easily single line—that is, on a direct, through basis—into California, into the Central Valley of that State, into Arizona, into Mexico, because they will have a big railroad that offers them excellent through service.

If a hypothetical lumber mill in the State of Washington today is served, say, by Union Pacific, as many are, Union Pacific can't even haul their freight to Arizona single line, or to places in California's Central Valley, like Bakersfield or Fresno. If it hauls it to Los Angeles, it has a zig-zag route back through Utah.

It cannot do better on its own but, in conjunction with SP, it could form a direct single line to link those sawmills in the Pacific Northwest to all the points in California, Arizona, and other areas.

Now, that point is very important when you then turn to the mills that are served, say, in Northern California and Oregon, by SP. SP is a weak, financially floundering business, and those mills, by dozens, are concerned not about the merger between Union Pacific and SP but with the possibility, which they regard as real, that SP will either cease to exist as a separate firm or will simply drift and provide them with a decreasing quality of service.

Now, the potential of merger, and I will end in 1 minute, in this situation is to place the shippers who now depend upon Union Pacific or Southern Pacific with much more expanded service, much more efficient service, and to put them on a competitive plane with their competitors who are served by Burlington Northern–Santa Fe.

If the UP–SP merger were to be denied, and I believe Mr. Fischer said something along that line, I'm convinced that UP will be unable to serve and to place its shippers in a position to compete with BN–Santa Fe shippers. Finally, there is a serious risk, fully appreciated by shippers and especially small shippers, that SP, on its own, would either drift aimlessly, providing them with poor service, or face its possible demise.

The merger of the Union Pacific and SP will deal with these problems, improve service quality, especially, I believe, for small

shippers, though it will favorably affect big ones, as well, and intensify competition, and that's the bottom line. Competition, but competition with benefits for shippers that they cannot get and would clearly forsake if this proposed consolidation were to be rejected. Thank you.

[Mr. Barber's statement may be found in the appendix.]

Chair MEYERS. Thank you very much, Mr. Barber.

Our final witness is Dr. Curtis Grimm. Dr. Grimm is a professor at the College of Business and Management at the University of Maryland in College Park, Maryland. As I understand it, Dr. Grimm, you will be using the map part of the time, so we'll try to hear you. Maybe you can use that mike at the end of the front table if you need to use the map when you're standing.

TESTIMONY OF DR. CURTIS GRIMM, PROFESSOR, COLLEGE OF BUSINESS AND MANAGEMENT, UNIVERSITY OF MARYLAND, COLLEGE PARK, MARYLAND

Dr. GRIMM. Thank you.

I very much appreciate the opportunity to be here today and to have direct input into the policy process on a very important matter. I've been conducting research on the issues we're discussing today for more than 15 years and specifically more than two dozen of my scholarly publications have dealt specifically with the railroad industry, mainly on deregulation, mergers, and competition issues.

My position on rail mergers remains as stated in a 1990 Brookings monograph, and I quote: "As Alfred Kahn and others have noted of the airline industry, it is important to recognize that deregulation did not authorize the Government to abdicate its antitrust responsibility and to fail to take actions to preserve competition. It is the ICC's responsibility to scrutinize carefully potential anticompetitive effects from both parallel and end-to-end railroad mergers. In particular, a policy of continuing to discourage parallel mergers appears to be in order."

In the remainder of my remarks today I'd like to elaborate on this position, basically that deregulation has provided substantial benefits but that rail competition must be maintained in order to preserve these benefits.

Now, deregulation of the U.S. railroad industry has indeed been a very successful policy, as others have noted here today. My 1990 Brookings study, which I think provides the most comprehensive analysis of the impacts of both rail and truck deregulation, finds that we have annual economic benefits from deregulation across these two industries of about $20 billion per year.

Why such large benefits from deregulation? Very simple. We substituted the free market for Government regulation. However, for the free market to function, we need strong competition. As I stated back in a 1984 article, "Rail intramodal competition must be encouraged in every relevant area. At stake are billions of dollars in economic benefits, as well as perhaps the very success of rail regulatory reform."

For shippers, more competitors equals lower rates and better service. For shippers, a reduction in the number of competitors from three to two or from two to one means higher rates and dete-

riorated service. In particular, smaller shippers need competition to ensure reasonable rates and service.

Will policymakers maintain sufficient rail competition? Well, we're at a critical juncture right now. Since the early 1980's, the U.S. railroad map has actually been relatively stable. We've had three large systems dominant in the East and four major railroads dominant in the West. Two of the Western railroads, Burlington Northern–Santa Fe, have recently merged, as has been mentioned. So, we're down to three railroads now in the West.

Now, I might note, and this is in response to an earlier question, I think by Senator Bumpers, railroad consolidations since 1980 have been predominantly end-to-end, not parallel. That's a very important point. In other words, they have not involved, by and large, mergers of direct competitors.

However, now we're very much at a moment of truth because the proposed Union Pacific–Southern Pacific merger is indeed a parallel merger. It's a merger of direct competitors. This isn't the forum to get into the details of that consolidation but I think that merger eliminates rail competition to an unprecedented degree, with competitive impacts, in fact, greater than the Southern Pacific–Santa Fe proposed merger in the mid 1980's which the ICC denied because of its enormous competitive problems.

Now, if we turn for a moment to the bigger picture, and that's the maps both on your left and right, the maps denote the combined market share of Class I railroads, the combined market share of Burlington Northern–Santa Fe system and the proposed UP–SP.

What kind of market share do these two railroads have in various regions of the West? Well, in fact, the magenta color that you see across the entire West denotes areas where these two systems will have fully 100 percent of the railroad market.

Further, there are some serious questions about how intensively these two railroads will compete, and I'll be happy to go into those if there are questions.

Now again, proponents of the merger suggest that two competitors are plenty and more than two are unnecessary. I strongly disagree. This runs counter to Department of Justice antitrust guidelines. It runs counter to common sense. Imagine our reaction if we were faced with a proposal that reduced the number of airlines or the number of any other firms in any other industry to just two. We'd say, "Well, that's just not enough." We should reject this idea for railroads in a similar manner.

Reduction of rail competition will have major impacts throughout the economy. Transportation, like telecommunications and other industries, we can think of as a strategic industry—it impacts performance and competitiveness of the entire economy.

For example, trade with Mexico is dependent on a competitive transportation system, and this merger would largely eliminate rail competition for United States–Mexico traffic. Again, we have another chart that shows rail market shares for United States–Mexico rail traffic, and we see that Union Pacific and Southern Pacific are the dominant two railroads with regard to United States–Mexico traffic. Burlington Northern is the third one.

Now quickly, with regard to policy options. I've long been a champion of policies to promote and preserve railroad competition. My written testimony and the references provided there give a lot of details.

But very importantly, more weight must be given to competitive effects in ICC rail merger decisions, and more deference must be given to the Department of Justice Anti-Trust Division's views in this regard.

Now, under current standards, the ICC could indeed approve a significantly anticompetitive merger based on claims of speculative efficiency gains, which could outweigh, in their view, competitive harms. The ICC is free to largely ignore the views of the Department of Justice, who are the acknowledged experts on competition issues, if it so chooses.

In sum, we're faced with a very serious reduction of rail competition. Congress should take appropriate steps to ensure rail competition is preserved. Thank you.

[Dr. Grimm's statement may be found in the appendix.]

Chair MEYERS. Thank you very much, Dr. Grimm. I have one question for you and then I think you did not ask questions the last time, so we'll go to Mrs. Smith and then Mr. Kennedy.

The question I have is: I have a memo in front of me that says that, "As a result of the Union Pacific–Southern Pacific proposed merger, 164 markets that are served by both railroads will now be served by the single merged railroad; whereas in the Burlington Northern–Santa Fe merger, only 16 locations went from two to one railroad." I would like your comments, Dr. Grimm, as to what that might do, and then Mr. Barber, you may want to comment on that also.

Dr. GRIMM. What you're detailing is what I was speaking of in terms of unprecedented anticompetitive effects of this merger and, in fact, far greater competitive effects than of the Burlington Northern–Santa Fe merger.

When we look at markets in terms of rail traffic between BEA areas we have a total, based on 1993 data, of about $1.65 billion worth of traffic that will be facing a complete elimination of rail competition with this merger. Again, that is about 10 times the magnitude as compared to the Burlington Northern–Santa Fe merger.

So, indeed this is amplifying what I'm talking about in terms of this being very different than previous mergers which have been approved by the ICC in the last 15 years. This is a parallel merger. The Union Pacific and Southern Pacific are direct competitors in many markets.

The settlement deal that's been struck by Union Pacific to give access to some of these shippers that are losing competition, give access to Burlington Northern, the second of the duopolists in the West, does not relieve those competitive harms in any significant way.

Chair MEYERS. Thank you. Mr. Barber?

Mr. BARBER. I don't know where those numbers came from but they are wrong in final result. At locations where UP–SP today provide the only rail service—that is, where the two of them serve and there's no other railroad—at every one of those locations, the

approval of the UP–Southern Pacific transaction, including the settlement that has been arrived at, will leave the shippers with the same choice of two railroads. That is, they will still have a choice of two railroads. The other railroad will be Burlington Northern–Santa Fe.

If we have a shipper at a location in California or Texas or someplace who today is served by UP–SP only, tomorrow that shipper at that location will be served by UP–SP as one choice and BN–Santa Fe as the other choice. The only difference is that the choices will be much better.

Chair MEYERS. I beg your pardon? Say that last sentence again, if you would, Mr. Barber. I didn't understand your last word.

Mr. BARBER. That the choice will be much better. Let me just briefly explain that. If a shipper at a location today has a choice between UP and SP, SP is viewed, and this, I think, is accurate to say in light of the hundreds of statements of shippers that will be submitted and be made public in about 3 weeks, those shippers regard SP as a very deficient choice. It is poor in service. It is deficient in its financial capacity, as it itself concedes. It has not been able to modernize.

The other point is that today if your choice is between UP and SP, your choice is, in terms of points you can reach in single line service, limited. For example, if somebody in Houston, a shipper, wants to ship something today and he's served by SP to a point in Arizona or New Mexico, he can't make the shipment. UP doesn't serve those States. It doesn't serve the Central Valley of California, just like SP doesn't serve Iowa or Minnesota or Wisconsin or the State of Washington.

So, the choice improves because SP and UP will be able to serve pretty much the entire West on a single line basis, but their alternative choice, BN–SF, will also be able to do so. So, choice improves at the two to one places at two to one locations, competition is preserved and enriched because the choice will be between two railroads, strong ones, financially well off, that will be able to provide single line service on a comparable basis throughout the Western United States. That, I think, is a real gain for competition.

Chair MEYERS. I appreciate your comments and I respect your great knowledge in this area. I also respect my sources to these figures, so somehow we will have to talk and make sure——

Mr. BARBER. I'll be happy to look at the memorandum that you referred to, if you wish to provide it.

Chair MEYERS. Thank you. Dr. Grimm?

Dr. GRIMM. This isn't the place to perhaps go into all the sordid details but suffice it to say that I would look at the competitive effects of this merger very differently from Mr. Barber. He's defining competitive effects very narrowly. He's not including at all competitive effects where you have railroads perhaps served just by Union Pacific or Southern Pacific but where the other railroad may be a few miles away. In Mr. Barber's calculus, that doesn't count as where we're losing competition.

But indeed, shippers that have a railroad a few miles away greatly benefit from the competition between those two railroads. They can threaten or actually transload by truck a few miles. They can perhaps relocate their plant. They can pursue perhaps an op-

tion of building a new rail line for a couple of miles or at least, again, threaten that to get a rate reduction and competition in negotiating for a contract.

So, that's just one example where I would be looking at a very important competitive effect in a given instance; Mr. Barber doesn't count it at all as a competitive effect.

Another example is where we might have three railroads in a given area, let's say in Houston, but for a shipper shipping from Houston to New Orleans, there are only two railroads, Union Pacific and Southern Pacific.

Now again, Mr. Barber doesn't count that as an area where you're eliminating rail competition but if somebody's shipping from Houston and they have a customer in New Orleans who wants their products, they have to ship to New Orleans. The fact that Burlington Northern travels from Houston up to the north doesn't help them at all.

A third way that we differ, just briefly, is that there's a whole array of customers, in fact $3.9 billion worth of traffic, where shippers' options will be reduced from three railroads to two railroads. Again, these three railroads are predominantly Union Pacific, Southern Pacific and Burlington Northern.

Now, I see that and I think the Department of Justice does, as well, in some of their preliminary comments, as a very serious competitive problem, as opposed to Mr. Barber's views. He sees that as actually pro-competitive because we have the two competitors rather than the three competitors.

So, that's just an example of the many ways that we're looking at this very differently. I would be happy to submit some further detail for the record that I think will help to clarify the differences in our views.

Chair MEYERS. Thank you. Mrs. Smith.

Mrs. SMITH. Thank you. I'm going to ask the two economists, because I'm getting more confused. I came to listen a lot today because the issue's been troubling to me. I'm a free enterpriser, but I'm having a bit of trouble when I realize that by their very nature trains have to be on tracks and there can only be so much competition in that.

I don't really understand the criteria or test the ICC uses to determine the effects of the merger or the anticipated effects, I guess you could say the antitrust effects on competition. You've talked about the Department of Justice. Could you describe the test the ICC uses, to be sure that the competition is there. Can either one of you clarify that? I'm still struggling with the issue of competition and the test that you do use when you're making the decision.

Mr. EMMETT. Mrs. Smith, I hate to get in between two dueling consultants. It's a dangerous place to be. But currently the ICC standards that are applied, they can consider competition but the overriding consideration is nearly always efficiency of rail service. Does this somehow improve the efficiency of the service?

Again, that goes back to 1980 when people were very worried that all the railroads were going out of business. There was even discussion of nationalizing the railroads and what were we going to do to maintain a strong rail industry? So mergers were definitely in order to preserve a rail system at all.

The Justice Department, under the current procedure, submits comments to the ICC, just like anybody else can comment. But the ICC is free to ignore those comments and to deal with competition in whatever way they deem appropriate.

There are many of us who now feel that the number of railroads has reached such a level that competition becomes an overriding concern and should be elevated even higher.

I might add at this point——

Mrs. SMITH. That would be by not allowing it to be advisory but a mandatory criteria?

Mr. EMMETT. Correct.

Mrs. SMITH. By the Justice system itself versus——

Mr. EMMETT. Well, our preference would be to have it go to the Department of Justice but even if it goes to the residual ICC, whatever that panel ends up being called at the Department of Transportation, they could be instructed by law to consider competition in a higher way.

I must add, and this is somewhat self-serving although I did not consider any mergers of Class I's in the 3 years I was there, the ICC has, over the years, enforced a law that's on the books to the best of their ability. You have the power to change that law and that's what a lot of us are here for today.

One other quick comment. I always find it amusing when people talk about, "These are the things we're going to do to help preserve competition for you, the shipper." I think in many cases the UP–SP merger, as it's been described, shippers will like, but in many other cases they may not like it.

I think what you need to hear from the people to my right, the people who actually put freight on the trains, is were they consulted? Were they brought into this process? Or where they told, "This is what we're going to do for you. It's good for you. Take it." And that's sort of an image that's been left out there.

Mrs. SMITH. Thank you.

Chair MEYERS. Thank you, Mrs. Smith.

Mr. Kennedy.

Mr. KENNEDY. Thank you, Madam Chair.

I want to echo something you just concluded with because I think the one theme that's going throughout all the testimony that I'm hearing today is the fact that we can talk in this political forum about one standard or another and the consultants, so to speak, can quibble about how they view a monopoly method of competition versus competition between two or more different companies, but the fundamental interest that we have on this side is the public interest. Clearly, when you're talking about our infrastructure and railways, they are a public interest.

So, in terms of competition, it really is important for us to guarantee that we don't have a system where the deck is stacked against the shippers, the small business shippers and anyone else, for that matter, because ultimately the buck gets passed down to the consumer, and they end up paying for inefficiency by virtue of the fact that there's a monopoly and someone can get away with charging as much as they want.

What I'd like to emphasize and what I've heard throughout the testimony is that we do need a process by which competition can

be evaluated. The ultimate test will be, what do these companies mean by efficiency. Do they mean just cutting people and laying people off and not reinvesting in their infrastructure and not charging a fair rate for the service that they provide?

These are things I haven't heard yet whether they have been included in the evaluation and measure of whether these mergers should go forward but I think they deserve an answer.

So, I would agree with you, in light of the ICC going away and in light of the fact that in this period in the history of the railways, that the very reason the ICC was created in the first place was to help mitigate the monopolistic tendencies that are currently under way through all these mergers.

We do need, through the Department of Justice, to come up with a measure that evaluates the lowest cost for transportation and not just the highest profits for corporate executives.

Now, the way I see competition—I've heard it told over and over—is we need to have the railways and the trackage rights listed in a public domain. You've got to start talking about the public domain. These tracks don't simply belong to the company that operates them. They belong to the American public and we have a vested interest in making sure that everyone gains access to these tracks.

The company that is most competitive is the one that wins at the end of the day and not the company that just manages to commandeer the public rights of way and use it for their own profit.

That's one of the things that I think is the reason the ICC was created, and I don't see this as simply an efficiency point of view from one company to the next on how much they can balance their own books. I see efficiency in that respect only after the public interest has been guaranteed through these rights of way so that you don't have the situation where these companies are having to get together and buy one another up so that they can buy the rights of way, because I think the rights of way belong in the public interest to the public. That's where I think we need to have a better evaluation of what this competition means.

I hope the Committee does take up some legislation to replace the function of ICC through an aggressive Department of Justice review so that we can cull these very sordid details, as Dr. Grimm referred to them, because this is obviously not the forum for those of us who are not experts in all the terms and the rest to be making those decisions.

But I think we can, in all fairness, make the decision that the public has a right to get the most competitive environment and that, I don't think, is served necessarily through a merger, these mergers and acquisitions that, in my view, have not been clearly presented to be the most cost effective way of getting the public interest met, where you have—and I'm concerned, quite frankly, that we're going to see a lot of people laid off. That's going to come under the guise of cost efficiency.

As I was talking to my colleague, Senator Bumpers, he's concerned about what kind of workers are going to get railroaded in this process and what kind of workers are going to lose their jobs. We need to have an answer as to what the profits are of some of these companies so that they're not just running away with a lot

of money that's gained at the sacrifice of the American public because we haven't done our job to ensure that there's proper regulation of this very important national assets, and that's our railways.

Finally, I just ask Dr. Grimm if he would comment on the evaluation—you talked an evaluation—what kinds of labor standards apply in these mergers and acquisitions and what rights are guaranteed to the workers in this whole process. Are they given any hearing, so to speak, at the table to have their voices heard, since they're the ones who are on the front lines, so to speak?

Dr. GRIMM. The whole——

Chair MEYERS. Proceed, Dr. Grimm, and then we will try to get our two final questioners in before we have to go and take a House vote.

Dr. GRIMM. Let me see if I can get something a little more detailed onto the record in response to that. There is certainly ample opportunity through the proceedings for labor to be heard, but let me, in the interest of time, respond to that in writing.

Mr. KENNEDY. Thank you.

Chair MEYERS. Thank you, Dr. Grimm.

Mr. Salmon.

Mr. SALMON. Thank you, Madam Chairman. I just have a couple of questions and the ones that I don't get to ask I would request the permission of the chair and the Committee——

Chair MEYERS. Without objection I would like to ask unanimous consent that all Members have the opportunity to submit questions in writing.

Mr. SALMON. Thank you very much. Madam Chairman, just a couple of quick questions.

First of all, I have to scratch my head every once in a while. I wonder are we in the Kremlin or are we in the Congress of the United States? I thought we believed in free enterprise and not always Government intervention.

I really appreciate the gentleman in the center—is it Mr. York? I appreciated your comments about keeping Government out of the equation. I think that's what this Congress is about, and letting the free market solve some of these differences.

I do have a list of the predominant shippers in my State, Arizona, and let me tell you the results. Basically 60 percent of them support the merger; the remainder are either undecided or neutral. So, I appreciate those of you that are shippers from other parts of the country but I have to react to those that—I dance with the ones that brung me.

I'd just like to ask a couple of questions of Dr. Grimm. Number one, Dr. Grimm, have you studied Southern Pacific's financial figures? Do you know what their cash flow was in the past 10 years?

Dr. GRIMM. Southern Pacific has not been very profitable. That's correct.

Mr. SALMON. In fact, they've lost $2 billion over the last 10 years and the only way that they've been able to stay afloat is by liquidating $2.3 billion worth of surplus real estate.

I wonder—you can comment if you'd like—as to what would happen to the small businesses if they went bankrupt. Then there is no Southern Pacific but the end result is that there are two competing railroads anyway.

I think this is a little bit short-sighted. Is your solution then that we subsidize Southern Pacific with taxpayer dollars to keep them afloat so that they can compete?

Dr. GRIMM. No. I would stress that I'm more free market-oriented than perhaps even you are. The free market does provide, even in the instance of a bankruptcy, with Chapter 11 procedures. Southern Pacific has some very valuable lines, many of them which are parallel to Union Pacific's in major corridors, which would definitely be acquired in that instance, if Southern Pacific went bankrupt. They would be acquired by competing railroads, railroads that would be pleased to extend their route systems, acquiring some of the very valuable lines that Southern Pacific now holds.

I think that process, again, if that were a scenario that came to pass here with a bankruptcy, we would not see reduction of competition; we would not see those track assets fade away; we'd see those track assets acquired by strong railroads that would provide a vigorous injection of competition and strong service into the region now served by Southern Pacific.

Mr. SALMON. Mr. Barber, would you care to comment? I have a hard time when we have consultants advocating bankruptcy. We've had some folks file bankruptcy in the State of Arizona. I won't comment on that right now but frankly, I'm not sure that's the—I'm sure that's an answer but Mr. Barber, would you care to comment?

Mr. BARBER. Yes, quickly. You are quite right in your supposition and in the predicate upon which you put the question to Dr. Grimm. SP is in terrible financial condition. It is surviving today only through what I call a process of self-cannibalization. It is living off of property sales. It is not able to generate capital from its internal operations. It is not and has not been able to invest in, among other things, the cars that the shippers want, the locomotives that they want, that they need, in the upgraded rail lines that are needed and especially in the line across Arizona, which is now terribly congested.

Mr. SALMON. I would agree. As I mentioned, the predominant group of shippers in my State are very supportive of this merger. But let me further—and I'll end because I know, in the interest of time, we've got to go vote—let me just say that I belonged to a Fortune 500 company before I came here. I was an executive for 13 years for U.S. West.

When we merged the three Baby Bells, the Northwestern, Pacific Northwestern and Mountain Bell, we found a tremendous increase, through the economies of scale, we found a tremendous increase in our productivity. Because we cut duplicative staffs, we cut out all those PR staffs and the human resources. There were numerous duplicative staffs. Through economies of scale we were able to become more efficient, more competitive, more effective, and delivered a better quality product to the consumer.

I don't buy this bull that by going from three to two and having two strong competitors, as opposed to one weak and two strong, that we're going to be harming the shippers. So, thank you very much.

Chair MEYERS. Thank you, Mr. Salmon. Mr. Poshard.

Mr. POSHARD. Thank you, Madam Chairman.

I guess the proof of the pudding for me, with respect to competition, and with all due respect to what the gentleman just said, if all of that is true, that going from three to two is more profitable for us as a Nation, all you people who said that by virtue of where you operate and mergers that have already occurred, your rates have gone up; why is that?

If all of this theory that you say is good from going from three to two and the competition, your rates ought to be going down. If we're developing an economy of scale and more efficiency in the process, you, Mr. Hoffman, ought to be paying less, not more. That's the bottom line and we all know that.

Where I live, where mergers have taken place, and the short lines have tried to take up the slack, we've got more logistical problems with the short lines trying to get cars, trying to integrate into the Class I railroads now; it's unbelievable, the mess that's occurred.

So, do we believe in competition? Absolutely. Should competition bring prices down for you people? Of course it should. If it isn't, something is wrong. I don't care what the theory and the textbooks say. The proof of the pudding is your rates ought to be lower and they're not where I live. I heard almost all of you say that they're not where you live.

So, we'd better take a hard look at this, Madam Chairman, in terms of what we're doing.

I'm sorry, I do have several questions but I don't want to miss this vote. It's very important. Thank you.

Chair MEYERS. No, I don't, either. I would like to say thank you to all of the witnesses. I think you have helped with our information gathering. We don't want this to go by without having a hearing in either the House or the Senate. We think it's extremely important and you have helped a great deal.

I don't know that legislation will result from this but I think it's extremely important that we hear about it from the small business point of view. I do know that Mr. Fischer feels strongly that he has been helped. He is a relatively larger shipper.

Those of you who are relatively small shippers, I think, are feeling very concerned about this and it's good that you had a forum to air those concerns and we will be very sensitive to that in the weeks ahead.

I thank you all very much for being with us.

[Whereupon, at 4:10 p.m., the joint hearing adjourned, subject to the call of the chair.]

APPENDIX

OPENING STATEMENT
CHRISTOPHER S. "KIT" BOND
JOINT HEARING ON IMPACT OF RAIL MERGERS
November 8, 1995

Thank you, Madam Chairman. I am pleased to join you once again as co-chair of a joint hearing of the House and Senate Small Business Committees, and I want to thank you for hosting this event. Just last week, we held a very successful joint hearing on our side of the Capital on the cost of regulations to small business. With today's hearing, the Senate is able to reciprocate, and join you here on the House side in this very lovely hearing room of the House Ways and Means Committee.

Today's joint hearing focuses on the impact of rail mergers on small shippers. It demonstrates the shared concerns of the House and Senate Small Business Committees with maintaining competitive rail service for small shippers. This is very much an "outside the Beltway" hearing. We are here today to listen to small shippers and learn from their unique perspective on recent and proposed rail mergers. Most of our witnesses have traveled here especially to testify before the Committees, and I would like to join Congresswoman Meyers in welcoming all of you to Washington.

Madam Chairman, several weeks ago, I was back in Trenton, Missouri, and had a chance to talk to Frank Hoffman who owns and operates a family run grain elevator. Frank told me of his concerns with the cost and quality of rail service, and how rail mergers were affecting the rail service to his elevator. It was clear from our talk that these issues not only affect elevator operators like Frank, but the hundreds of farmers who depend on the local grain elevator to get their corn, soybeans and wheat to market.

This situation is typical of grain elevators throughout Missouri and much of the Midwest. Many of these elevators are totally dependant on rail transportation to get their product to market and to import fertilizer at competitive rates. Today, the committee is going to get a chance to hear more about the effects of rail mergers on a typical, small-sized grain shipper from Phil Hoffman, who is Frank's nephew. Phil, I want to welcome you to the committee and I look forward to your testimony.

Since my initial conversation with Frank Hoffman back in Trenton, I have heard from many other small shippers who are worried about how their rail service might be affected by mergers and other consolidations. These small shippers have a vital interest in maintaining high quality and competitively priced freight rail service in this era of mega-mergers in the rail industry. While they recognize that these mergers present opportunities for more efficient rail service, they are also concerned that these mergers may adversely affect small shippers. I hope today's witnesses will provide the committee with a clear picture of both the potential benefits and problems presented by these mergers.

Madam Chairman, I am delighted we have joined together to provide small shippers with an opportunity to bring their concerns to the attention of Congress. I want to thank you again for hosting this hearing, and look forward to today's testimony.

Statement
Senator Dale Bumpers
Joint Hearing Before the Committees on Small Business
of the
House of Representatives and the Senate
November 8, 1995

I want to commend the two chairs for scheduling our second joint hearing in as many weeks with our House colleagues on an issue which vitally affects my state. Railroad mergers are very serious business, and it is appropriate that the Small Business Committees should examine the impact on small shippers of the largest proposed railroad merger in living human memory between the Union Pacific and Southern Pacific companies. The continued availability of competing rail lines is vital to many small shippers and to towns large and small across my state.

Both of these railroads and their predecessors have played huge roles in the history and economy of Arkansas, as in many other states. Union Pacific and Southern Pacific own and operate tracks which enter Northeast Arkansas from Southeast Missouri and parallel each other in a southwesterly direction until Southern Pacific's tracks split toward Shreveport and Dallas, while Union Pacific's tracks head south toward Houston. Union Pacific also bisects Arkansas in the opposite direction from Fort Smith southeast to Louisiana, and both railroads have connections to Memphis. I ask consent that a map of the Union Pacific and South Pacific systems be included in the record.

In addition, Union Pacific operates a large maintenance facility employing 1600 workers in North Little Rock, while Southern Pacific employs 900 people at its rail yards and repair shops in Pine Bluff, only 47 miles away. There are presently

2,669 Union Pacific jobs and 1,206 Southern Pacific jobs in Arkansas. Simply looking at the map and seeing the obvious parallel of these two lines, it is difficult to imagine that none of these jobs will be affected by the proposed merger. The United Transportation Union has written to me expressing its opposition to this merger, and I ask that a letter to me from Mr. Don Beavers also be included in the record following my statement.

There has been discussion of trackage rights for the Burlington Northern-Santa Fe Railroad over the Southern Pacific tracks which, in Arkansas, mostly means the old Cotton Belt line. Trackage rights, however, can be essentially a landlord-tenant relationship.

It seems quite possible that many towns in Eastern and Southern Arkansas will eventually go from two rail carriers to one, if the merger is approved.

Additionally, a competing offer for the Southern Pacific lines has been made by Conrail which currently has no presence in our part of the country. If accepted, the Conrail proposal would link Conrail's extensive Northeast network with Memphis, Dallas, Houston, New Orleans, and eventually Mexico, and it appears that all of that traffic would pass through Arkansas. Conrail has discussed the possibility of building a major maintenance facility in Pine Bluff, or perhaps expanding the existing Southern Pacific shop. There may be other parties' offers which should be considered as well.

While I have not come to any firm conclusion about the merits of the merger proposal, I look forward to learning more from today's testimony. Although

Union Pacific has rejected the Conrail proposal to buy Southern Pacific's eastern lines, I believe this offer should be carefully considered by the ICC or whatever agency eventually has responsibility for approving this merger.

There are some potentially positive aspects to this merger which must be considered, as well. One is the access that Missouri-Pacific shippers' would have to Southern Pacific's southern corridor. This stretch between El Paso and Southern California could eventually become available through a single carrier.

Railroad mergers have historically been within the jurisdiction of the Interstate Commerce Commission whose days seem to be numbered. Railroad mergers have been judged by standards different than strictly competitive harm, which generally rules the day under Section 7 of the Clayton Act. It has sometimes taken the ICC years to decide the outcome of rail merger proposals, and the Commission has power to set appropriate conditions on the approval of any merger.

The future venue of this important area of law may be decided by a markup in the Commerce Committee later this week. Whatever the outcome, I hope the final decision maker will carefully weigh the many factors involved in this case, including the testimony which we will hear today. If they have not already done so, I ask that the two Committee Chairs arrange for today's hearing record to be transmitted to the Interstate Commerce Commission as soon as it is complete.

Again, I thank Chairmen Bond and Myers for convening this hearing, and I thank the witnesses for their time and their comments.

STATEMENT OF REP. JAN MEYERS (R-KS)
CHAIR
HOUSE COMMITTEE ON SMALL BUSINESS

JOINT HEARING
HOUSE COMMITTEE ON SMALL BUSINESS
AND
SENATE COMMITTEE ON SMALL BUSINESS

November 8, 1995

"RAILROAD CONSOLIDATION: SMALL BUSINESS CONCERNS"

At the outset, I would like to welcome our colleagues from the Senate to the House side of "the Hill" for our joint hearing today. The subject of today's joint hearing is railroad mergers and their impact on small business, particularly small shippers.

Not too long ago, in 1980, there were 42 Class I railroads operating in this country. If the mergers already approved, announced or heavily rumored this year are completed, there will be only 8 Class I railroads left in this country -- at the beginning of this year, there were 12. Please do not mischaracterize my concern. I am sure that many of the Class I rail mergers that have occurred in the past 15 years were not only necessary, but were clearly pro-competitive. Our primary concern for today's hearing is the recent trend toward mega-mergers among previously competing Class I railroads and how these mega-mergers affect small business shippers, particularly shippers of bulk commodities such as agricultural goods.

As our first witness we have with us today a former colleague and a fellow Kansan, Secretary of Agriculture Dan Glickman. After Secretary Glickman's testimony we will have a brief round of questioning. Following our questioning of Secretary Glickman, we will hear from our second panel today. We will have 8 witnesses on our second panel who are intimately familiar with the issue of large rail mergers and how they impact small shippers.

One small housekeeping matter before we begin. Chairman Roberts of the House Committee on Agriculture is unable to be with us today, but he would like to submit a statement for the record. [Without Objection] Furthermore, without objection, I would like to keep the record of this hearing open for ten days to receive statements of other colleagues and interested parties who are not with us at today's joint hearing.

Statement of

REP. JOHN J. LaFALCE

Committee on Small Business

Hearing on "Railroad Consolidation: Small Business Concerns"
November 8, 1995

The Committees' examination this afternoon of the potential impact of railroad mergers on small business shippers comes at a time when many people believe the United States has turned the corner and overcome its decline in competitiveness. I have my doubts about that proposition, and I believe we must review the trends in railroad mergers and acquisitions in this light.

The railroad industry was the first major nationally regulated industry in the United States, and, in part, the Interstate Commerce Commission was established for this purpose. The recent merger activity we are witnessing results from the national trend toward deregulation. The underlying rationale for such deregulation is to promote competition within and among industries, to provide greater choice to consumers, and to increase efficiencies and productivity. Deregulation is one of the tools thought by some to promote the U.S. competitive position in the global trade arena.

It appears that deregulation has to some degree spawned a more dynamic railroad industry. At the same time, however, mergers and acquisitions have reduced the number of rail lines in the industry to the point of creating what we could term "shared monopolies."

If the Union Pacific-Southern Pacific merger is approved, it will be the largest railroad west of the Mississippi--and it will share the territory with the Burlington Northern-Santa Fe which is now number one with $7.8 billion in revenues. Recently, Union Pacific concluded an agreement with Burlington Northern to grant tracking rights to nearly 4,000 miles of rail lines--if Burlington Northern does not oppose the UP-SP merger. This to me sounds like monopolistic behavior--not the route to a more competitive environment for the railroad industry and its customers.

A truly competitive environment will offer customers more options for shipping their goods to markets. Recent experience indicates that they have fewer options--and sometimes only one option.

A truly competitive environment would allow other participants in the industry to enter the market--more railroads competing for shippers' business. So far, the opposite is occurring, and the monolith railroads are pushing out the smaller railroads.

A truly competitive environment would push costs down for shippers. In fact, costs are rising because lack of competition allows the "shared monopolists" to set prices without competing price pressures.

In order for the United States to be trade competitive, its industries--large and small--must be competitive. They must have access to easy, reliable, and cost-effective transportation services. The nation's railroads are a central element of such services. We as policymakers make a mistake if we do not

recognize the long-term damage we inflict to our businesses and the nation's economy if deregulation results in anticompetitive practices.

Madame Chairman, thank you for holding this joint hearing on such an important issue for small-business shippers. If we are to support correct economic policies, we must anticipate the consequences of actions before they are taken. There can be no more important issue for small business than the national transportation system on which it relies.

Statement of Senator Tom Harkin
Joint Small Business committee hearing on
Railroad Consolidation: Small Business Concerns
November 8, 1995

The recent, and pending, mergers of major railroads will have substantial a impact on coal, industrial and farm commodity shippers. While these mergers may allow the rail industry to become more efficient, there are also likely to be losses in competition. When the number of class I railroads with the effective ability to move grain in a major geographic area of the country is less than a handful, real competitive problems are likely to occur. Shippers, particularly smaller shippers, have real fears of being unfairly treated.

The indications of the Union Pacific's policies towards modest sized shippers is cause for concern. Their announced and possible future actions concerning loadings for grain of 50-car and smaller trains may have extremely negative impacts on both the viability of individual grain elevators and on the price that farmers will receive for their grain.

With the almost certain elimination of the Interstate Commerce Commission, considerable care must be taken by the federal government to examine carefully and limit the negative impacts of rail mergers. This is a time when real care needs to be taken to consider the many significant effects that could occur. A fair and efficient mechanism for the adjudication of rate disputes is needed.

The Chicago Northwestern was the largest railroad in Iowa until it was recently taken over by the Union Pacific. Clearly, it is too early to know what the ramifications of the merger will be on my state's commerce. At the present time, there is a major shortage of rail cars -- particularly grain cars. In large part, this shortage has been caused by a shift of barge traffic towards nonagricultural goods. As a result, railroads have been forced to move grain all the way to ports such as New Orleans rather than to barge terminals on the Mississippi River. The recent merger of the UP and CNW has exacerbated the situation. I understand that whole trains of loaded grain have sat for many days in Iowa because of coordination and staffing problems.

We need to increase our capacity to move goods in the barge system and improve the availability of rail cars. We also need to find ways to treat small shippers fairly without creating unreasonable limitations on a railroad's operating methods.

I look forward to acquiring information in this hearing that will be helpful towards these goals.

**STATEMENT OF SENATOR LARRY PRESSLER
SENATE COMMITTEE ON SMALL BUSINESS
AND
HOUSE COMMITTEE ON SMALL BUSINESS
JOINT HEARING ON
RAILROAD CONSOLIDATION: SMALL BUSINESS CONCERNS**

NOVEMBER 8, 1995

As a Senator from South Dakota whose economy is based primarily on agriculture and small businesses and as Chairman of the Senate Committee on Commerce, Science, and Transportation, the impact of mergers on small shippers obviously is of great concern to me. The trend toward increased concentration of the largest railroads heightens this concern. However, Class I concentration is not the only dynamic within the industry.

As the Class I's continue to get bigger and bigger, and fewer in numbers, development of smaller short-line and regional railroads increases. To a large extent, the concerns of small shippers often mirror those of the small railroads. Together they both are often dependant on a single Class I for car supply, market access, switching rights and other fundamental matters.

All parties in discussions over these kinds of issues have legitimate concerns. These concerns need to be better defined in order to resolve them on any permanent basis in this rapidly changing industry. I think it is entirely possible for the industry to resolve these issues, and encourage that process. Done correctly, it could provide more effective relief to legitimate small shipper concerns and be far less problematic for Class I's than any government imposed solutions.

There should be no doubt the Commerce Committee perceives the small shipper concerns as very real. There is a definite problem. It must be addressed. We have made that point emphatically clear in the Interstate Commerce Commission sunset legislation. Indeed, the bill as introduced provides a mechanism for resolving these kinds of issues. If the industry does not chose to employ the opportunity in a constructive manner, those resisting reasonable efforts to address legitimate concerns through industry compromise are likely to face a far less favorable outcome in the form of a government solution.

Finally, I emphasize that in my view the primary problem is for the small businesses -- both shippers and railroads. Throughout the ICC sunset legislation process and continuing today in other forums, it seems to me other interests are quick to use small business as a means to achieve their agenda. I intend to remain vigilant to ensure operators are not used as fronts for someone else's agenda. I encourage the same vigilance for others attempting to explore these legitimate concerns of the small shippers.

Congressman Pat Roberts
Chairman, House Agriculture Committee
Wednesday, November 8, 1995
Senate and House Small Business Committee
Joint Hearing: "Railroad Consolidation: Small Business Concerns"

Thank you. Mr. Chairman, Madame Chairman. I share your concern for the future of small business and rural America and applaud your committees for taking up the difficult and important issue of captive shippers.

As Chairman of the House Agriculture Committee, I have worked to ensure that the nation's agriculture industry remains strong. Those of us who come from rural districts know well the impact agriculture has on the entire economy.

While I realize this committee does not have jurisdiction over the shutdown of the Interstate Commerce Committee (ICC), I fear that agriculture is in for a rough ride. Captive shippers have fallen into double jeopardy. The railroad industry is consolidating into large companies and the ICC, once a mighty regulatory body, is preparing for shutdown.

While much has been said of past and future rail mergers, I do not believe it is the purpose of Congress to make determinations on private companies. With that in mind, however, we have an obligation to speak up

when Kansas' grain shippers are in danger.

In Kansas, the agriculture industry is dependent on railroads to deliver their products. Virtually all grain products shipped out of Kansas go by rail. If rates increase as a result of noncompetitive railroads, the economy in farm country will surely suffer. As the agriculture industry can not pass on increased costs of service, farmers will bear the brunt of rate increases. Historically, farmers have paid this bill in terms of price, convenience and efficiency.

Several issues must be addressed:

- **Rate Notification.** Agriculture shippers need advanced rate notification. Shippers base their grain prices for farmers in large part on anticipated transportation costs, which account for 10 to 30 percent of the value of agricultural products at their destination. Without advance public notice of rate changes, the marketplace cannot operate efficiently and fairly.
- **The Common Carrier Obligation.** This provision, which requires carriers to serve all rail users on an equitable basis, must be preserved with effective equipment limitations and anti-discriminatory provisions.

We are at a crossroads. Regardless of whether we want it or not, change is coming. The market is global and we operate on economies of scale. All sectors of the economy must change to face the growing challenges of a global and competitive marketplace.

However, it is essential that we plan now to make that change orderly so that rural America has access to transportation needed to stay competitive in this new marketplace.

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STATEMENT OF SENATOR PAUL WELLSTONE
JOINT HEARING OF THE COMMITTEES ON SMALL BUSINESS
NOVEMBER 8, 1995

MADAM CHAIR AND MR. CHAIRMAN. Thank you for holding this timely hearing on a topic that is very important to my state.

I am especially pleased that we have the Secretary of Agriculture here today. Minnesota has been experiencing what the executive director of our state's Farmers Elevator Association has called a "crisis" in grain transportation this year.

I would like, if I could, to place two items into the record of today's hearing. The first is a statement from the Farmers Elevator Association of Minnesota.

The second is a set of articles from the Des Moines Register, written by George Anthan just a couple of weeks ago. George is one of the finest agriculture reporters in the country, and, for the benefit of Committee staff, I'd like to submit the text of these articles on a disk. I understand that facilitates the printing of these transcripts. The articles describe clearly a portion of the situation that we are here to examine today: the dramatic consolidation in the rail industry and its potential impact on farmers and small shippers.

I hope this hearing can begin to clarify the extent to which mergers and concentration in the rail industry might be contributing to some of the difficulties that Minnesota farmers and elevator operators have had in getting their grain to markets this year. I am sure that I am not the only member of Congress whose constituents in agricultural areas see this not only as an acute problem today, but potentially as a serious issue in coming years.

At the very time that we are moving toward removing ICC regulation of this industry, problems are emerging that may be due to economic concentration. The problems have been of two kinds, both serious: problems of availability of transportation, and problems of the cost of transportation.

We have had a very wet fall in Minnesota - a lot of rain and significant snowfall already. I can tell you that no one in Minnesota wants to see piles of grain stored on the ground through the winter, especially when we know there are markets for that grain and that world prices are strong.

We are a country whose agriculture has benefitted from the best infrastructure in the world. Agriculture can benefit from efficiencies in the transportation sector and from the cost savings that can result from efficiencies. But we also have to have real competition that helps preserve the rights of shippers. And we need either incentives or requirements that ensure that our rural communities have access to the country's transportation

infrastructure.

Transportation is the economic lifeline of rural America. I intend to explore with the Secretary and others the issue of how we can ensure that there will be adequate oversight of the transportation sector in the future.

I look forward to the testimony, and to being able to ask some questions.

Thank you.

STATEMENT OF

RICHARD J. BARBER

COMMITTEES ON SMALL BUSINESS

OF THE UNITED STATES CONGRESS

November 8, 1995

My name is Richard J. Barber and I am a transport economist. Over the last 30 years I have dealt extensively with transportation -- and particularly rail transportation -- in many different capacities: as a member of the staffs of Congressional Committees, as a Deputy Assistant Secretary for Policy at the U.S. Department of Transportation from 1967-70, as a consultant to the Senate Commerce Committee when it was coping with the aftermath of the collapse of Penn Central (and other railroads in the Northeast and Midwest), and as a private consultant to railroads (including Union Pacific), truckers, and bargelines, some of them big, some small.

Thirty or so years ago the American railroads were generally not performing well. Their sheer numbers were large but they were geographically fragmented. While truckers could carry goods door-to-door in efficient single-line moves, extending to hauls of a thousand or more miles and connecting points anywhere in the country via the Interstate highway network, railroads

could not then do so. They had to hand off their shipments from one to another to still another, in an inefficient interlining process that retarded quality of service and was detrimental to the interests of shippers. Railroads, as a result, were losing market share and were deeply troubled financially.

Today the railroads generally are performing much better, offering improved, more competitive service to shippers. For example, in the Southeast the creation by merger of the expanded Norfolk Southern and CSX systems now pits two strong railroads against each other in a vigorously-contested market environment. This is a good illustration of the public benefits of rail consolidation. Inherently railroads are inflexible enterprises, committed to physical networks laid out decades ago that do not mesh well with the needs of our modern economy. Individually they lack the scope of operations -- the market breadth and routes -- that allows them to serve the great breadth of shipments with the single-line service that best meets customer requirements.

Consolidation in this industry is the most effective means of achieving conformance with the contemporary marketplace. The proposed merger of Union

Pacific (UP) and Southern Pacific (SP) -- like that of Norfolk Southern and CSX and the recently-approved combination of Santa Fe and Burlington Northern (BN) -- reflects the same objective: better, expanded single-line service. And it will lead to the same result: increased, not lessened competition, to the benefit of shippers, of all sizes, for all products, throughout the West. The UP-SP consolidation poses no threat to competition. Quite the opposite: it will promote competition.

Shippers of all sizes will benefit from the UP-SP consolidation, but smaller shippers will realize substantial gains because they are highly dependent on the railroad serving them. Big shippers, for example, may be able to satisfy their car requirements by supplying their own equipment, but small companies typically rely on the railroad -- just as they rely on their phone company for communications whereas a bigger company could create its own customized service. Small shippers -- bigger ones as well -- depend on their railroad for access to the market and the better that service the more successful they can be in building sales and creating jobs in their local communities.

For shippers the UP-SP consolidation promises immense benefits of many different types --

(1) New shorter, faster routes than those presently available over the two roads. These will provide better, more competitive service for shippers moving goods:

between	and
the Pacific North West	Kansas City
California	Chicago
Texas/Louisiana	St. Louis
Arizona/New Mexico	Houston
the South East	New Orleans
the Central Mid West	Salt Lake City
the Upper Mid West	Denver
the South West	Seattle
	Memphis

as well as in other heavily-used corridors. This means quicker, more reliable transit times and more efficient use of freight cars -- meaning enhanced car supply.

(2) Expanded single-line service north-south along the Pacific Coast from the Canadian Border and Washington/Oregon/Idaho/Montana, through California, and into Arizona and the South West; for the movement of grain from the Mid West to SP destinations in California, Arizona, Texas, and Mexico; for lumber moving from SP origins to UP points and from UP origins in the North West to SP destinations; and for freight movements between the many points that neither UP nor SP can connect today (e.g., the Twin Cities and points in Arizona or California such as Fresno and Bakersfield).

Consolidation will weld together into a single-line network all locations which UP and SP do not both now serve. This will put UP and SP, and their shippers, on more nearly-level competitive footing with Santa Fe/Burlington Northern and their shippers.

(3) Expanded investment in upgraded routes and new or additional intermodal terminals in California, Memphis, Chicago, and other locations.

(4) Greater Efficiency achieved through better integration of lines, terminals, and related facilities. The resulting economies, greater than those produced by any prior rail merger, will be reflected in lower rates as well as in better service for shippers.

Consolidation also will rescue SP shippers from that railroad's severe service and financial problems. SP is a very troubled railroad. It is not generating the cash needed for capital investment from its operations and is surviving through property sales. Its poor service quality reflects its underlying weakness -- and, indeed, its long-term viability as an independent railroad. Consolidation removes this dark cloud and combines its routes with those of UP in a complementary fashion that will improve service to shippers on both of these railroads.

Finally, competition will be improved by the consolidation. Shippers now served only by UP or SP, and no other railroad, will suffer no loss of competition -- instead they will gain expanded single-line access, via better routes, to all UP and SP points. For shippers now served by both UP and SP, and no other railroad, the consolidation assures them of a continued competitive rail choice -- via Santa Fe/Burlington Northern, which offers the most expansive service in the West. And for shippers now having a choice between UP, SP, and a third railroad, the quality of choice is improved.

Today shippers at these locations have as their alternatives a financially-strapped and service-deficient SP; a route-inhibited UP; and a very strong, well-positioned Santa Fe/Burlington Northern. Post-consolidation they will be much better off -- with an option between two strong, comparably-positioned railroads, UP-SP and Santa Fe/Burlington Northern. As has been the case in the Southeast and in the Pacific North West -- areas where two railroads compete fiercely -- this spells stronger competition and far better shipper options than those which UP and SP can presently provide.

Disapproval of the UP-SP consolidation -- or the effective equivalent: dismembering it and distributing its essential interwoven components among other railroads -- would be anti-competitive and squarely contrary to the interests of shippers and the public. SP and UP customers would be denied the benefits of expanded single-line service and placed at a disadvantage compared with those of their rivals who are served by Santa Fe/Burlington Northern. SP would be left adrift, imperiling its shippers. UP would continue to be handicapped by inadequate routes and suppressed coverage of the West. The result would be to ensconce Santa Fe/Burlington Northern's position as the dominant railroad in the region.

The UP-SP consolidation is overwhelmingly pro-competitive. It offers a vast array of solid public benefits and when the formal application is submitted to the Interstate Commerce Commission on December 1 it is expected that hundreds of shippers -- big and small, from many different industries, geographically diffuse in location -- will urge its approval.

BEFORE THE
JOINT HEARING OF THE
SENATE SMALL BUSINESS COMMITTEE
AND THE
HOUSE SMALL BUSINESS COMMITTEE

Impact of Rail Mergers on Small Business

November 8, 1995

COMMENTS OF
THE NATIONAL INDUSTRIAL TRANSPORTATION LEAGUE

Edward M. Emmett
President
The National Industrial Transportation League

My name is Edward M. Emmett and I appear today as the president of The National Industrial Transportation League. The National Industrial Transportation League is the nation's oldest and largest broad-based shippers' organization. The League represents shippers of all types and sizes. Our members use all modes of transportation in domestic and international commerce.

Over the past few years there has been much debate about the future of the Interstate Commerce Commission and its functions. One of the major functions of the ICC, the handling of railroad mergers, is of major interest to shippers. Therefore, we appreciate the opportunity to appear today.

The League has had a long association with the Commission. In fact, the League was formed in 1907 in response to passage of the 1903 Elkins Act which extended jurisdiction of the ICC to rail shippers as well as railroads and the 1906 Hepburn Act which strengthened the authority of the ICC. Over the past 87 years, the League and its members have had constant contact with the Commission. On a personal note, my contact has been very close. I served as an ICC Commissioner from 1989 until 1992.

When asked to evaluate the ICC and its responsibilities, I must say it is a matter of perspective, much like the tale of the blind men who were asked to describe an elephant. Each man touched a different part of the animal—one the leg, another the tail, and yet another the floppy ear. Their descriptions varied greatly. This animal called the ICC also produces a variety of descriptions, from dinosaur to sleek efficiency.

The League perspective is that of the consumers of transportation services. It is two fold. In a simplistic sense, no transportation mode or system should exist without the support of shippers. If the

consumers do not want or need to utilize a form of transportation, there is no reason for it to continue. Also, in circumstances where a shipper has no alternative but to use a particular mode, or perhaps even a particular carrier, there needs to be a referee to insure fairness.

Throughout the debate over sunset of the ICC, the League has strongly endorsed moving the review of rail mergers to the Department of Justice. In the review of rail mergers, the League strongly endorses the use of antitrust laws and not the current rail merger provisions of the Staggers Act.

The Staggers Act provisions were written some 15 years ago with an entirely different set of circumstances in mind than that which exist today. In 1980, there were 42 Class I railroads. Today there are 10, and of those there are six major railroads—and two of those are currently the subject of a merger. The Staggers Act merger provisions were intended to encourage an industry on the verge of bankruptcy to merge into economically viable companies that could compete with each other and with other modes of transportation. For the most part, the goals of the Staggers Act have been achieved.

No one can argue that today's U.S. rail industry is on the verge of collapse. This is perhaps, the golden era of the freight railroad. Service is better than ever and still improving. The industry is innovative and is investing in the future. More and more freight is being moved by railroads. The economic strength of today's railroads is evidenced by the prices paid for the Santa Fe and offered for the Southern Pacific. This is not an industry near bankruptcy. It is a strong vibrant industry. Rail mergers should now be judged by the same antitrust considerations as other U.S. companies seeking to merge.

While rail mergers are similar to mergers in other industries, they are not exactly the same. Many

shippers who must use rail service are served by only one railroad. These shippers are captive and must be protected from anticompetitive market conditions. If Exxon and Texaco were to merge, consumers would still be able to drive to another service station to buy gas. Rail shippers, however, can only use the railroad that comes to their plant.

The Staggers Act has been very successful in re–developing a profitable, private freight railroad system. Its administration has failed, however, to promote rail–to–rail competition. Instead, policies have been adopted that allow carriers to erect barriers to competition. Its rail merger provisions have also out lived their usefulness.

Assuming that the Union Pacific/Southern Pacific merger is allowed to take place, the western two–thirds of the United States will be served by only two major railroads. Within two to three years, we predict that there will only be two or three major carriers serving the entire U.S. unless Congress acts now to change the way rail mergers are reviewed.

We are at a critical juncture in U.S. rail transportation policy. It is essential that the Congress act now to change the standards for judging rail mergers to focus more on competition. These changes must apply to the proposed, but yet unfiled, merger of the Union Pacific and Southern Pacific railroads.

Under the current statute, the ICC can find a rail merger to be completely anticompetitive, yet still approve it because it produces rail efficiencies and the Department of Justice cannot challenge the merger as anticompetitive in court. Taken to its extreme, the ICC or its successor could allow only one railroad in the U.S. because it would produce efficiency. Clearly, such a situation is not in the best interest of the U.S. shipping public.

The League urges Congress to make the following changes to the Interstate Commerce Act during the ICC Sunset debate:

1. Require that railroads compete with one another and not just with other modes of transportation.

2. Change the rail merger review process to focus on the anticompetitive aspects of a merger, and to provide the Department of Justice a more direct role in the rail merger process.

3. Require that any agreements between railroads regarding trackage rights, overhead rights, and haulage agreements be made part of the public record.

4. Require the proposed, but yet unfiled, merger of the Union Pacific and Southern Pacific railroads to be conducted under these new guidelines.

The League continues to support moving the review of rail mergers from the ICC or its successor to the Department of Justice. Short of that, however, we support the approach taken by Congress with regard to bank mergers. In bank mergers (12 U.S.C. 1828(c)) the regulatory agency has authority over the merger, but the Department of Justice is given specific authority to review the merger and, if the regulatory agency does not adequately address the anticompetitive aspects of the merger, Justice may challenge the merger in court. Under the current Interstate Commerce Act, Justice may file comments like any other party to the merger and the ICC can choose to incorporate those comments or not. If the Commission approves the merger without addressing the anticompetitive concerns of Justice, the

Department can only challenge the decision on the grounds that a material error was made, they cannot challenge the merger on antitrust grounds.

It is important that the UP/SP merger be reviewed under the new statute. The Congress has determined that the ICC will cease to exist after December 31, 1995. The Congress should not allow these two railroads to rush their merger proceeding before a lame duck agency so that their merger can be reviewed under friendlier terms. If the Congress wants to address the problems of competition and maintain more than two railroads in the United States, then no more major mergers should be reviewed under the current statute.

The League has been an active participant before the House Transportation and Infrastructure and Senate Commerce, Science and Transportation Committees throughout the ICC sunset debate. We are anxious to work with you to preserve and enhance the protections for business brought about by competition.

Thank you for this opportunity.

BACKGROUND MATERIALS

Rail-to-Rail Competition: 49 U.S.C. 10101 should be amended by adding the following: "to encourage and promote competition among rail carriers in order to maintain reasonable rates by rail, to promote efficiencies in the provision of rail service, and to provide expeditions remedies for traffic and facilities lacking effective transportation competition."

DOJ Participation in Bank Mergers:

1. Banks that wish to merge submit their applications to the responsible bank regulatory agency (Federal Reserve Board, Comptroller of the Currency, FDIC, or Office of Thrift Supervision). The agency then sends a copy of the application to the Department of Justice for a competitive factors report.

2. DOJ reviews the proposed transaction to determine whether it raises substantial anticompetitive concerns. If an initial review determines that there is no competitive concern, the Department sends a letter to the agency stating this conclusion.

3. If the Department concludes that the merger does raise competitive concerns, DOJ must send a detailed statement of these concerns to the regulatory agency.

4. If the regulatory agency approves the merger or acquisition, it must immediately notify the Department of Justice. The Department then has 30 days following the agency

approval within which to file suit to enjoin a merger or acquisition as an antitrust violation.

5. Under the Bank Merger Act, filing of the antitrust suit automatically stays the merger or acquisition until the judicial resolution of the suit, unless the court shall otherwise specifically order.

6. The bank merger is protected from antitrust challenge by government or private parties if the Department of Justice does not challenge the transaction within 30 days after the bank regulatory agency has approved the merger.

Testimony
By
Mr. Duane "Butch" Fischer
President, The Scoular Company
before the
Joint House and Senate Small Business Committees
November 8, 1995
2:00 P.M.

Good afternoon, Chairman Bond, Chairwoman Meyers, and members of the Committees. Thank you for giving me the opportunity to testify before you today. My name is Butch Fischer. I am President of The Scoular Company, a diversified agri-business concern headquartered in Omaha, Nebraska. I have been with The Scoular Company for 23 years in various capacities, primarily grain merchandising-related positions, until becoming company President in 1990.

The Scoular Company actively trades grain and grain by-products throughout North America. Our company physically handles 65 million bushels of grain through company-owned facilities in Missouri, Montana, Kansas and Nebraska. We also are involved in trading 300 million additional bushels.

Our grain shipping facilities are located throughout the West. All but two are rail served.

Grain Shipping Facilities	Transportation
Butte, MT	Union Pacific RR (UP)/Montana Rail Link
Sidney, NE	UP, Burlington Northern RR (BN)
Salina, KS	UP, BN
Herman, NE	Truck
Venango, CO	BN
Lamar, NE	Truck
Elsie, NE	BN
Madrid, NE	BN
St. Paul, NE	Nebraska Central
Brandon, NE	BN
Harrisonville, MO	Missouri & No. Arkansas
Archer, NE	BN
Hershey, NE	UP
Sutherland, NE	UP

We also have merchandising offices in Omaha; Overland Park and Salina, Kansas; Indianola, Iowa; Orchard Park, New York; and Sarasota, Florida. These offices handle more than 75,000 carloads annually. In addition, we transload approximately 20 million bushels per year in destination markets such as Texas, Utah and California. Our bulk transload sites are located in California, New Mexico, Texas, Missouri, Oklahoma, Alabama, Florida, Pennsylvania and New York.

Our by-product volume exceeds one million short tons annually, including corn gluten feed, dried distillers grains, hominy feed, whole cottonseed, and wheat millfeed.

Transportation in crucial to our business. Rail transportation is especially important in our grain trading activities. We own or lease 557 covered hopper cars that we operate on both eastern and western rail carriers. We ship over 20,000 hopper carloads annually. In our fiscal year 1995, we paid nearly $51 million for rail transportation of grain including shipments on Union Pacific and Southern Pacific. We use other modes of transportation,

as well. We paid $13.25 million for truck shipments and over one-half million dollars for barge transportation.

Scoular's traffic flows primarily from grain surplus states in Nebraska, Iowa, Kansas, South Dakota, North Dakota, Colorado and Montana to domestic processors, feed mills and exporters throughout the United States. As noted above, our largest facilities are served by Union Pacific as well as Burlington Northern. Therefore, I am well acquainted with railroads and their role in businesses like mine - - one that deals in bulk commodities and depends on efficient rail service.

Having told you about my company, allow me to again express my appreciation for being invited to share my views on past and future rail mergers, especially those involving Class I railroads, and the impact those mergers and consolidations have on small businesses that ship by rail. As you can tell from my description of The Scoular Company, we are not a small business. However, we merchandise the fruits of the labor of the ultimate and original small business, the family farm, and related agricultural entities.

I have observed the consolidation of the rail industry first hand over the past two decades. In the early 1980's Union Pacific, Missouri Pacific and Western Pacific were combined into one rail system which was then capable of competing more effectively with Burlington Northern. Later Union Pacific acquired the Katy (the Missouri, Kansas and Texas Railroad). This brought not just physical expansion of the system, but also improved operating efficiencies that enabled grain shippers to have access to more markets, both domestic and export. More recently, Union Pacific has completed its acquisition of the Chicago and North Western Railway which is currently being fully

integrated into Union Pacific's operations. Meanwhile, the Burlington Northern/Santa Fe have begun implementing their merger which was just approved last August. Finally, as you know, Union Pacific is preparing to file its application with the Interstate Commerce Commission for approval of its acquisition of the Southern Pacific.

The number of Class I railroads has declined but the remaining railroads today are more efficient, more productive and better able to serve grain shippers, large and small. Railroad mergers have resulted in more market outlets for grain grown in the geographic vicinity of these Class I railroads and the regional and short-line railroads that have been created from lines that the Class I railroads can no longer afford to operate. The larger railroads resulting from mergers also are capable of making more resources available to move grain. They also have a better understanding of the needs of their grain customers. Without the rail mergers of the last two decades the rail transportation infrastructure for grain would have remained fractured and balkanized. Consolidations have created opportunities for grain producers and merchandisers to find new markets for their products.

The broader the market reach of a railroad, the more effective it is at offering grain merchandising opportunities. This, in turn, increases the value of grain to both the producers and the merchandisers. That translates to more revenue potential for all of us in the grain industry.

Do railroad mergers mean that railroads can charge their customers whatever the railroads want for transportation? Clearly, the answer is "no." The forces of competition, both source and product competition in grain markets, compel railroads to remain

competitive in rates. Otherwise, foreign sources or sources of grain in regions that a particular railroad cannot reach will get the business, instead of that railroad's shipper.

Certainly problems may arise from time-to-time but they are transitory. Cars will be in short supply at harvest time. Systems integration at time of consolidation will produce some short-lived problems; but, once the short term problems are overcome, the benefits of rail consolidation are tremendous.

For example, when the integration of the CNW into Union Pacific is complete UP operations will be more reliable and efficient. Reductions of car handling at interchanges will make schedules faster, increase reliability and improve service. These improvements will enhance our ability as a shipper to serve our flour milling customers in the East over the Chicago and St. Louis gateways. The UP and CNW are now better able to compete over those gateways than they were as individual railroads.

Single- line service between the Upper Midwest and Mexico via CNW and UP offers new sources of supply for our Mexican customers. These sources were not practical before the merger. Single-line service improved the competitive position of UP and CNW shippers by allowing UP/CNW the same economies their competitors enjoy.

None of the recent rail mergers of Class I railroads (Burlington Northern/Santa Fe, Union Pacific/Chicago North Western or Union Pacific/Southern Pacific) has reduced or will reduce rail competition from any of our facilities. In fact, some of the markets in which we trade have more effective competition than they did prior to these rail mergers.

Some mergers in some industries may well present problems for small businesses. However, each merger, especially each rail merger, must be examined on its own merits.

Small businesses need efficient and reliable rail service because they simply cannot afford lengthy delays in delivery of and payment for their goods. They often need to rely on prompt delivery because of limited storage capacity or the need to minimize inventory related costs. Grain shippers in particular need to reach a wide variety of markets as economically as possible.

The pending merger of Union Pacific and Southern Pacific is an excellent example of a merger which will produce more competition for grain products throughout the United States. Utah, Arizona and California are all destination markets for grain that will be more competitive after the UP/SP merger than before. Simply put, the UP/SP merger is a rail consolidation that presents a wide array of benefits. The combined UP/SP system will provide improved service and expanded markets as a result of new single-line or more direct routing.

- Midwest grain and grain product producers served by Union Pacific will have improved access to SP grain and grain markets in the Pacific Southwest and western Mexico.

- New single-line access from U.S. border gateways to Canadian barley sources will be available for SP receivers in California. Also, single-line service from Idaho and Montana to California will open additional markets.

- New single-line service opportunities will be especially significant for shippers to Mexico. UP/SP will have improved single-line routes and access to all major border crossings into Mexico. This will create flexibility for export shippers and allow them to take advantage of the growing Mexico markets.

In addition to single-line efficiencies, combining routes, facilities and traffic of both UP and SP will create a more efficient carrier with fewer bottlenecks. Congestion will be reduced at consolidated terminals, like Kansas City and Houston. Larger volumes

and pre-blocking of traffic will allow shipments to avoid congested yards altogether in some cases. The elimination of intermediate handling permits shipments to move faster thereby reducing costs and increasing reliability. Shippers benefit also by dealing with only one railroad, rather than two or more, for pricing, customer service and car tracing.

An example of these service benefits for our company will be the access our Butte, Montana, facility will have to the dairy feed mills in the Central San Joaquin Valley that are now serviced by the SP. Currently, we can only access about 20% of the California market on a UP direct basis. Additionally, our facility in Salina, Kansas, will have access to SP-served destinations.

Along with better service and expanded market opportunities will come better equipment utilization. The equipment benefits from the UP/SP merger can be summarized as follows:

- Expanding use of the shuttle train program to SP-served California/Arizona receivers will improve overall equipment utilization, availability, and productivity.
- There will be increased opportunities for triangular movements of covered hoppers. As an example, from May to August, feed grains move from UP Midwest origins to SP receivers in the Southwest (Arizona and Southern California) and wheat moves from the same Southwest area to the Gulf and Midwest.
- Overall reduction in transit time due to more efficient and direct routes will provide the opportunity to manage equipment more effectively.
- Equipment supply due to complementary peak seasons for covered hopper grain shipments.

Improvements in equipment supply and car availability are important in the grain industry whether they result from fleet expansion or improved utilization. Whatever the reason, it

translates into savings for those of us who have our own cars. We need to invest less in railcars as a result of greater efficiencies.

Add to all of the above the fact that a larger, financially stable UP/SP will be more efficient and advanced in communications, car tracing and information technology and can serve its customers better than SP. SP's weakened financial condition has impaired its ability to compete. In our experience UP is distinguished by its ability to work with customers to supply quality service at competitive prices. The UP marketing people are adept at putting together programs large and small to serve their customers. On the basis of past performance, we believe the UP will provide top-notch service for all their shippers, large and small, if the UP/SP merger is approved.

Direct competition is important. Where two railroads compete head - to - head with each other, shippers enjoy the benefits of price and service competition. That competition should be maintained wherever it exits today. That is precisely what UP/SP plan to do in their merger. They have entered into an agreement with Burlington Northern/Santa Fe which will be an integral part of the UP/SP merger. That agreement will preserve competition at every location where UP and SP are the only two railroads serving a shipper today.

We are not troubled by the reduction in the number of Western railroads as a result of the UP/SP merger. SP's weakened financial condition has left it an ineffective competitor. SP's role in grain transportation has been insignificant. After the UP/SP merger, there will be even stronger competition between UP/SP and the BN/Santa Fe. Both rail systems have already demonstrated their ability to battle one another in the

marketplace. That intense level of competition will be increased after the UP/SP merger when the agreement with BN/Santa Fe also takes effect.

As you undoubtedly know, the UP/SP merger will benefit BN/Santa Fe shippers. Specifically, BN/Santa Fe shippers will gain new service options as the result of the agreement reached with UP/SP. That agreement will provide BN/Santa Fe with a new central corridor route from Denver to the West Coast, a new direct single-line route from the Pacific Northwest to California and new routes between Houston and Memphis and between Houston and New Orleans. BN/Santa Fe will also obtain new trackage rights to the Mexico border crossings at Eagle Pass and Brownsville, in addition to access to the Laredo gateway via a connection at Corpus Christi. These new routes available to BN/Santa Fe once the UP/SP merger is approved will benefit Midwest grain shippers. This is just another reason why my company enthusiastically supports the UP/SP merger.

I am certainly not alone in this view. I understand that UP/SP have the support of a significant and growing body of shippers, both large and small. UP/SP will file with their application, I am told, more than 1,000 statements of support for the merger from shippers who, like me, have taken their time to describe the benefits we expect to experience from the UP/SP merger. Among those 1,000 plus shipper statements will be numerous statements from grain shippers and receivers, as well as other agricultural interests throughout the United States, who want the ICC (or its successor) to know that the UP/SP merger will benefit all of the U.S. economy.

'e ⁻believe that the proposed UP/SP merger would be in our company's best
; as well as the interests of other shippers. We heartily endorse the UP/SP
We believe that this merger is good for all businesses, big and small.

hank you for the opportunity to present you with my views. I will gladly answer any
s you might have.

United States Department of Agriculture
Statement of Dan Glickman
Secretary of Agriculture
Joint Hearing of House and Senate Committees
on Small Business
on
Railroad Consolidation: Small Business Concerns
November 8, 1995

Committee Chairs and Members of the Committees:

I am pleased to be here today to discuss small business concerns with the growing consolidation of the United States railroad industry.

The continued success of American agriculture depends on maintaining an effective and efficient railroad industry. This is particularly true in large areas of the Midwest, where inland waterways are not nearby and distances to market are great. While American grain farmers bear the ultimate burden, there are over ten thousand local country grain elevators and dozens of smaller, regional railroads whose profitability is fundamentally linked to access to a competitive U. S. railroad industry.

I am deeply concerned with the trend towards increased consolidation and concentration in the rail industry. Within the agricultural community, there is great concern that the increased consolidation and market power of large railroads could lead to increased cost and decreased availability of rail transportation services to rural America as well as decreased efficiency of grain marketing in the United States. It is unclear whether this would occur. If this does occur, it would have a substantial adverse effect on agricultural income and the entire rural economy, and I applaud the efforts of these Committees to take a hard look at these issues.

Importance of Rail Service to U.S. Agriculture

Rail service is critical to the economic well-being of most agricultural and rural communities in the United States. Reliable, cost-effective transportation of agricultural products enables U.S. agricultural producers and shippers to be competitive in both domestic and export markets. I cannot overemphasize the importance of maintaining U.S. export markets. This year, the United States will have record agricultural exports, and we project continued export expansion in a growing world market. Rail transportation is essential for American agriculture to be successful in meeting this increased world demand.

Nearly half of all grain produced in the United States moves to market by railroad. In 1994, grain, grain mill products, and other farm products accounted for about 2 million rail carloadings. Also in 1994, agricultural shippers paid 2.7 billion dollars in freight costs to U.S. railroads to move agricultural products from country, subterminal and terminal elevators in grain producing areas to domestic and international markets.

Specific grains and regions are even more dependent upon rail transportation. Nine of the ten top wheat-producing states are more than 150 miles from barge transportation on the Mississippi River which typically provides the strongest intermodal competition to railroads on the long distance movement of grain for export. Among agricultural shippers in the United States, wheat shippers in the Upper and Lower Great Plains have practically no transportation alternatives to railroads. The wheat produced in these areas moves long distances to domestic markets for processing and consumption or to coastal ports for export. Shippers in these regions have little direct access to inland waterway transportation and the distances involved make truck transportation uneconomical.

To illustrate the dependence on rail transportation, I would note that nearly 80 percent of all interstate wheat shipments from the Plains States are by railroad, and rail accounts for 90 percent of all export traffic from the region. Rail is also the dominant mode of transportation for interstate shipment of wheat -- accounting for 80 percent of such shipments in the Upper Great Plains States and more than 60 percent of the intrastate shipments in the Lower Plains States.

Effect of Increased Railroad Concentration

Railroad mergers and consolidations of the past few years continue a dramatic structural change which began over the last twenty years. There are now twelve Class I railroads in the United States, down from eighteen Class I carriers in 1988. Several years ago, two of the top four grain hauling railroads merged when the Union Pacific (UP) was granted authority to acquire the Chicago and Northwestern Railroad. This summer, the Interstate Commerce Commission (ICC) approved the merger of the Burlington Northern (BN) and the Atchison, Topeka & Santa Fe (ATSF) railroads, creating the largest railroad system in the United States at that time. The combined BN-ATSF system is massive and extends from the Canadian to Mexican borders and from the West Coast into the Southeastern United States. In terms of U.S. agriculture, the BN-ATSF merger consolidated the Nation's two largest wheat hauling railroads.

The consolidation of major railroads is continuing. In August 1995, the Union Pacific Railroad (UP) announced its intention to purchase the Southern Pacific (SP) railroad, which is the largest U. S. railroad. If this latest railroad consolidation is approved, there will only be two major rail carriers west of the Mississippi. This could have serious implications for the rates and availability of rail transportation for the agricultural industry because of the reduced level of competition.

Moreover, nationwide statistics can mask potential market power by merged railroads in more specific geographic markets. For example, the combined BN-ATSF system leaves just two railroads controlling nearly all of the wheat shipments to Kansas City and account for over half of all wheat delivered to the Texas Gulf for export. The potential for collusive behavior in a host of other geographically-specific markets will also increase as the number of competitors decreases to either two or three railroads.

As major railroads have restructured through mergers or consolidations and abandonments, rural rail service has been preserved in many instances by the formation of small or shortline railroads. Throughout the 1980's and continuing today, regional and local railroads have become increasingly important to agricultural and rural communities by assuming service to rural areas which had been discontinued, or which was about to be discontinued, by Class I railroads. Today, small railroads continue to play a vital role in supplying farm communities with raw materials and farm inputs and in facilitating the marketing of the agricultural production of rural and agricultural areas.

Large railroad mergers and consolidations cause great concern among these small and regional railroads, the viability of which is heavily dependent on car supply and service from Class I railroads. While some small railroads and their shippers have long complained of less than equitable treatment by their Class I connections, consolidation in the rail industry increases concern among small railroads and their shippers about the future viability of small railroads. For example, the Burlington Northern/Atchison, Topeka and Santa Fe merger has generated apprehension and concern among rail shippers located in Kansas, and shippers across the country are concerned about the proposed UP/SP merger.

Common concerns of these smaller railroads and their shippers with increased consolidation include the potential for a growing number of captive shippers who are only served by one railroad, reduced service, noncompetitive rates, and car ordering systems that cannot be used effectively by small businesses, most of which are country grain elevators.

Finally, increased consolidation in the U.S. railroad industry greatly concerns U.S. agriculture because of the clear connection between the adequacy of rail service for grain shippers, income received by farmers, and the competitiveness of U.S. grain exports in the world market. As a recent USDA study demonstrated, inadequate railcar service leads to lower prices for farmers and higher prices for foreign buyers -- leading to both lower farm income and a reduced competitiveness of U.S. grain exports in world markets. While inadequate rail service affects shippers and smaller railroads, U.S. farmers bear the greatest risks of railcar supply problems through lower farm prices and lower export volumes.

This year the lack of available railcars is causing serious problems in some areas of the country like Iowa and Minnesota, where large amounts of grain are being stored on the ground. This will not only reduce farm income as the quality of the grain deteriorates, but it comes at a time when we are experiencing record tight grain supplies.

The Future of Agriculture and the Railroad Industry

The 1995 Farm Bill is likely to increase the importance of competitive rail service for U. S. agriculture. In addition to reducing farm program spending, the 1995 Farm Bill will likely provide U.S. farmers with much greater planting flexibility. This fundamental transformation in U.S. farm policy will require farmers to respond more to international and domestic markets. Given the reliance that U.S. farmers will be placing on the availability of markets for their farm income, we must be especially vigilant about concentrations of market power in rail transportation. Increased consolidation could adversely affect the efficiency of the U. S. agricultural marketing system and ultimately lead to a reduction in farm income. To enable farmers to realize the benefits of a market-oriented farm policy and continued expansion of U. S. agricultural exports, a cost-effective railroad transportation system must be available.

In addition to debating the 1995 Farm Bill, Congress is currently considering legislation to eliminate the Interstate Commerce Commission (ICC), a goal which the Administration strongly supports. The Administration's legislative proposal (H.R. 1436) retained some of the current regulatory oversight of the railroad industry and provided for Department of Justice review of proposed railroad mergers under the Clayton Act standards.

Given the increased market power of railroads, the agricultural community strongly believes that some form of federal regulatory oversight of railroad pricing, practices and mergers must be continued. While the Administration and Congress may not agree about the best way to provide for this oversight and protect captive shippers, we can agree that failure to provide any oversight could have serious repercussions on U.S. agriculture and the entire rural economy, the economic viability of which is highly dependent on the railroad industry.

Conclusion

U.S. agriculture has greatly expanded productivity and profitability over the past fifty years. Today, as we move towards a market-oriented farm policy and expanded international trade, we need to ensure that U.S. farmers have a marketing system that provides a competitive return for their production. Fundamentally, that means a marketing system in which railroad transportation services are adequate and competitively-priced. As Secretary of Agriculture, I look forward to working with these Committees and the entire agricultural and transportation communities to achieve this important goal.

I will be glad to answer any questions you may have at this time.

United States
Department of
Agriculture

Agricultural
Marketing
Service

Transportation
and Marketing
Division

Marketing and
Transportation
Analysis

September 1995

Assessing the Impact of Railcar Availability on Grain Prices

United States
Department of
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September 1995

Assessing the Impact of Railcar Availability on Grain Prices

Jerry D. Norton, Economist

Abstract

This study uses empirical data to evaluate the effect of railcar availability on grain price spreads between country and export markets. Three distinct rail markets for export grain were identified and included in the analysis: 1) wheat moving from Kansas, Oklahoma, Texas, Colorado, and Nebraska to the Texas Gulf, 2) wheat moving from Idaho, Montana, North Dakota, Oregon, and Washington to the Pacific Northwest, and 3) corn moving from Minnesota, Nebraska, and South Dakota to the Pacific Northwest. The relationship between grain price spreads and railcar availability proved to be statistically significant and negative, indicating that as the availability of railcars decreases, the spread or difference between the export market price and the country price increases. The study concludes that increases in price spreads caused by reductions in railcar availability and railcar shortages lower farm prices and reduce the competitiveness of U.S. grain exports.

Keywords: Grain price spreads, railcar availability, railcar shortages

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Summary

Analysis in this report uses empirical data to evaluate the effect of railcar availability on grain price spreads between country and export markets. To examine this relationship, a model of grain price spreads between country and port positions is defined and estimated. The model includes variables to control for shifts in export grain demand, local grain supply, and rail transportation demand. It also includes variables to account for changes in elevator handling costs and transportation rates. Binary variables are included to account for regional, seasonal, and crop variations in price spreads. Most importantly, the model includes a variable that indicates changes in the level of railcar availability over time.

The scope of the model is restricted to those States and terminal export markets that rely extensively on rail transportation. Three distinct markets are identified and included in the analysis. The first market is defined for wheat moving from Kansas, Oklahoma, Texas, Colorado, and Nebraska to the Texas Gulf. The second market is defined for wheat moving from Idaho, Montana, North Dakota, Oregon, and Washington to the Pacific Northwest. The third market is defined for corn moving from the western Cornbelt States of Minnesota, Nebraska, and South Dakota to the Pacific Northwest. The regression coefficients and equation are estimated using monthly data for the period 1986–89.

The estimated equation is significant and explains 72 percent of the variation in the price spreads. Taken individually, the signs of the coefficients for each variable are consistent with what would be expected based on traditional economic theory. Local supply, export demand, elevator handling costs, rail rates, and rail demand are positively related to the price spread. The positive relationship between these variables and the price spread indicates that as the variables increase, so do the differences between port and country prices. Export demand and elevator handling costs are significant at the .01 confidence level. Rail rates are significant only at the .10 confidence level. Local supply and rail demand are not significant at ordinary levels of confidence. Railcar availability is significant at the .01 confidence level. Unlike the other variables in the model, railcar availability is negatively related to the price spread, indicating that as the availability of railcars decreases, the price at the terminal market rises relative to the country price, thus increasing the price spread.

Elasticities of price spread with respect to the variables in the model are also calculated. The elasticity of price spread with respect to railcar availability is inelastic, but indicates that changes in railcar availability can have substantial price spread effects. Based on the elasticity estimated at the mean values for the variables in the equation, a 1,477 change in the daily average balance of available railcars would result in a 1 cent change in the price spread for wheat or corn in the study markets. This level of variation in railcar availability is small in comparison to the range of 16,244 to –5,287 that was observed in the variable during the 1986–89 study period. In fact, within a range of plus or minus 1 standard deviation (a range in which more than two-thirds of all the observations fall), grain price spreads could increase or decrease by as much as 5.6 cents per bushel.

Given that domestic supply is more inelastic than domestic or export demand, the largest share of the change in price spread is borne by U.S. producers through the prices they receive for their grain. Increases in grain prices at the port, which can result from widening price spreads, should also be of concern as they raise the price of U.S. grain in world markets. Such price increases reduce the competitiveness of U.S. grain in the world market, and make alternative sources more attractive to foreign buyers.

Introduction

Supply and demand conditions in the transportation market influence the ability of the grain market to price grain over time and space and, consequently, to move grain from producers to consumers. In the long run the interaction between the transportation market and the grain market is reflected in the general level of grain prices. In the shorter run this interaction is reflected in adjustments in price differences for grain between points in time and location. These adjustments reveal much about the underlying market conditions for grain and transportation, and they provide the market with the signals necessary to guide participants to longer-run market equilibriums.

The existence of highly active cash, cash-forward, and futures markets allows grain to be rationed efficiently over time and space. Both of these dimensions are captured in the basis, which is defined as the difference between the futures price and the local cash price. Because the basis is determined by a futures price and a cash price unique to one location, the basis includes components of both time and space. The space component of the basis can be isolated by taking the cash terminal market price at a specified futures delivery point and subtracting the local cash price.

Price differences between various cash grain markets reflect the spatial relationships that exist in grain supply and demand. Fundamental economic theory tells us that prices in areas of abundance will be low relative to prices in areas of scarcity. It is this price difference, and the opportunity to profit from it, that spurs the movement of commodities.

The spatial price differentials, or spreads, that exist between country and terminal grain markets normally reflect the costs associated with handling and transporting grain between the two points. For any two markets which actively trade grain, the largest component of the price spread should be the cost of transportation. In the long run, transportation cost is determined by the underlying supply and demand conditions in the market for transportation services. In the short run the price of transportation may not fluctuate with sufficient freedom to stimulate the market responses necessary to allocate equipment based on its marginal value to shippers. This is particularly true for rail transportation, where the market has traditionally been characterized by limited intermodal and intramodal competition and a subsequent reliance on public policy to regulate pricing and service.

Given this feature of rail transportation, it is useful to study how supply and demand conditions in the rail transportation market affect the market for grain. The purpose of this study is to assess how price spreads between grain markets respond to changes in the supply and demand for the railcars used to haul grain. Since rail transportation supply can be constrained by institutional and pricing inflexibilities rather than market forces, it is particularly useful to evaluate these grain price responses during periods when prevailing transportation demand exceeded available supply, as in the 1986–89 study period.

Rail Transportation and Grain Price Spreads

Grain price spreads between terminal and country markets are a function of the cost of moving grain. In markets dominated by rail transportation, rail rates represent a large portion of the price differences. Through the analysis of spatial price relationships, economic theory and existing literature provide a framework from which to evaluate the impact of rail transportation supply and demand on grain marketing. Theory also provides insights into how grain market participants are affected by imbalances in rail transportation supply and demand.

Grain Price Spreads

The U.S. grain market closely approximates the theoretical model for a perfectly competitive market. Grain is a homogenous and easily standardized commodity. Participants in the market are free to enter and exit with little restriction. A sufficiently large number of buyers and sellers exist such that no individual buyer or seller is able to significantly affect the behavior of the market.[1] Although knowledge may not be equal or "perfect" among market participants, price information is generated and reported instantaneously through futures market and cash market transactions. An abundant and timely supply of information allows grain markets to respond quickly to changes in supply and demand conditions.

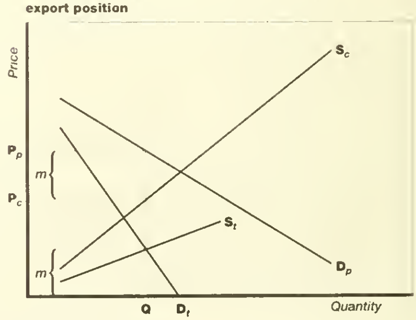
The grain market's close approximation of the perfectly competitive model provides a framework from which to assess the relationships between grain prices in different geographical markets. Spatial price differentials in markets which trade and where competitive conditions exist are determined largely by the cost of transfer between the markets. Such transfer costs include loading and handling, as well as the actual transportation cost or rate.[2] Factors beyond transfer costs can affect price differentials in markets that diverge from the conditions of perfect competition. Davis and Hill classified the causes of price variability among local country elevators as: 1) differences in availability and costs of transportation, 2) differences in operating costs, 3) differences in local demand and supply conditions, and 4) market power.[3]

Terminal-to-country price spreads are the result of transfer costs and differences in supply and demand conditions in the two markets. In the aggregate, differences in local elevator operating costs and market power may be assumed to have small or even negligible effects on the overall level of terminal-to-country price differentials. When price spreads are examined over sufficiently broad geographical regions, adequate levels of competition should exist to generate elevator operating costs that are at their marginal levels. The larger number of selling firms in the broader region should also minimize any of the effects characterized as localized market power by Davis and Hill. Differences in the cost and availability of transportation, however, are directly reflected in the terminal-to-country price spreads through their impact on transfer costs.

Figure 1 conceptualizes the classic derived demand model under which grain price spreads are determined. In figure 1 and for this analysis, the terminal market is identified as the export elevator or port position. The supply function for grain in the country is represented by *Sc* and the demand function for grain at the port is represented by *Dp*. The demand for transfer services is derived from the interaction between the *Sc* schedule and the *Dp* schedule and is shown as the function *Dt*. The supply of transfer services is given by the market as the function *St*. The intersection of *Dt* and *St* determines the quantity of transfer services and grain (*Q*); the cost of transfer or margin (*m*); the price of grain in the country (*Pc*); and the price of grain at the port (*Pp*). The price spread between the country and port is *Pp–Pc*, and equal to *m*.

Transfer services which facilitate the movement of grain from the country to the port include those costs associated with storing, handling, and transporting grain between the two points. The significant level of capacity and competition that exists in the storage and handling of grain should result in per unit costs for storage and handling that remain relatively fixed over a wide range of quantities. At any given time, with respect to price spreads, storage costs are essentially reduced to zero. Handling and transportation thus account for the difference in prices between geographical locations. Handling costs, however, are small relative to transportation costs for most shipments. Given this, the upward sloping supply curve for transfer services in figure 1 implies an upward

Figure 1
Grain price spreads between the country and export position



[1] Dale C. Dahl and Jerome W. Hammond, *Market and Price Analysis: The Agricultural Industries* (New York, NY: McGraw-Hill, Inc., 1977), p. 287.

[2] William G. Tomek and Kenneth L. Robinson, *Agricultural Product Prices* (Ithaca, NY: Cornell University Press, 1972), pp. 143–144.

[3] L. Davis and L. Hill, "Spatial Price Differentials for Corn among Illinois Country Elevators," *American Journal of Agricultural Economics*, vol. 56 (1974), pp. 135–136.

sloping supply curve for transportation services. A smooth, upward sloping supply curve for transportation is accurate only to the extent that transportation supply and price can adjust to changes in supply and demand. This qualification is especially important for rail transportation given the regulatory environment in which it operates.

Rail Rates and Grain Price Spreads

The Staggers Rail Act of 1980 greatly increased carrier flexibility in rate making. Prior to Staggers, railroad rates were established collectively through rate bureaus. This joint rate-making process restricted the ability of carriers to set individual rates or service agreements. Rates adjusted slowly to changes in the market.[4] The Staggers Act allowed rail rates to adjust much more quickly. New tariff-filing requirements were adopted that reduced the amount of time required to implement rate changes. Staggers also provided rail carriers and shippers with the ability to negotiate rate and service contracts. These two changes did much to increase the potential for rail rate flexibility.[5]

Increased rate flexibility combined with decreases in export grain demand in the early half of the 1980's to substantially reduce rail rates for grain in many regions of the country. Klindworth et al. found that Kansas-to-Gulf rates for wheat that increased on average by 10 percent during the 1977–81 period, decreased by 40 percent during the 1981–84 period. These rate reductions were generally thought to be passed on to producers as higher prices and to consumers as lower costs. This was shown to be true for Kansas wheat when rail rates decreased in the early part of the 1980's.[6] Sorenson suggests that rate flexibility, however, increased the rail rate volatility for Hard Red Winter wheat.[7]

Movement toward a more flexible rail rate-making system should contribute to increased price uncertainty for grain at the farm level. The supply of grain at the farm level is more inelastic than either domestic or export grain demand. For this reason, Koo points out that farmers would be expected to bear the larger portion of the adjustment in rates that results from rate flexibility.[8] As the transportation rate that separates terminal and country markets becomes increasingly flexible, farm-level prices should also become increasingly more uncertain.

Adam and Anderson found that the uncertainty associated with country elevator bids for soybeans and corn in Nebraska increased following the Staggers Act. Their analysis relied on the changes in the futures-to-country basis to test for farm-level price uncertainty.[9] Such basis changes are confounded by factors related to time and transportation. Later analysis, based solely on farm prices for corn, failed to support this conclusion. Sarwar and Anderson concluded that some of the transportation-related causes of farm price uncertainty prior to Staggers were replaced with new causes of uncertainty following passage of the act. Price uncertainty caused by flexible rates replaced price uncertainty that resulted from chronic railcar shortages prior to Staggers.[10,11]

Common among research in the early and mid-1980's is the hypothesis that increased rate flexibility, while adding to grain price uncertainty, would be offset by reductions in the uncertainty associated with railcar availability. This was central to Johnson's arguments for deregulation in the early 1980's. Johnson argued that railroads had reduced rates in reaction to surplus car conditions, thus preventing the idling of cars that would have occurred prior to Staggers. He suggested that flexible rail rates would allow railroads to avoid capacity surpluses and shortages.[12]

In practice, the ability of railroads to avoid surpluses and shortages is dependent upon their ability to quickly adjust supply or rates as market conditions change. Wilson found that modal shares for rail shipments of North Dakota grain were consistent with the theoretical model of dominant firm price leadership with sticky prices.[13] He asserted that rail rate price "stickiness" was, in part, the result of the method by which rates were traditionally regulated.[14] Sarwar and Anderson believed that railroads were unable to take full advantage of seasonal and demand-sensitive rate making because of the depressed demand for rail transportation in early post-Staggers years.[15]

Railcar Availability and Grain Price Spreads

Rail deregulation under the Staggers Act was specifically aimed at improving the profitability of financially ailing rail carriers. It was believed that increased rate flexibility would make railroads more competitive with barge and truck transportation by allowing rail carriers to adjust rates and services to meet changing market conditions.

[4] L.O. Sorenson, "Some Impacts of Rail Regulatory Changes on the Grain Industry," *American Journal of Agricultural Economics*, vol. 66 (1984), p. 646.

[5] S.J. Fuller, J. MacDonald, D. Bessler, and M. Wohlgenant, "Effect of Railroad Deregulation on Export Grain Transportation Rate Structures," *Texas Agricultural Experiment Station Bulletin* (College Station, TX: Texas A&M University System, Texas Agricultural Experiment Station, 1988), B-1583, p. 2.

[6] Keith A. Klindworth, L. Orlo Sorenson, Michael W Babcock, and Ming H. Chow, *Impacts of Rail Deregulation on the Marketing of Kansas Wheat* (Washington, DC: U.S. Department of Agriculture, Office of Transportation, 1985) p. 29.

[7] Sorenson, p. 650.

[8] W.W. Koo, "Impacts on Agriculture of Deregulating the Transportation System: Comment," *American Journal of Agricultural Economics*, vol. 65 (1983), p. 188.

[9] Brian G. Adam and Dale G. Anderson, "Implications of the Staggers Rail Act of 1980 for Level and Variability of Country Elevator Price Bids," *Journal of the Transportation Research Forum*, vol. 26 (1985), p. 363.

[10] Ghulum Sarwar and Dale G. Anderson, "Railroad Rate Deregulation and Uncertainty of Farm-Level Prices for Corn," *American Journal of Agricultural Economics*, vol. 71 (1989), p. 890.

[11] Ghulum Sarwar and Dale G. Anderson, "Impact of the Staggers Act on Variability and Uncertainty of Farm Product Prices," *Proceedings—Twenty-seventh Annual Meeting; Transportation Research Forum*, vol. 27, no. 1 (1986), pp. 148–149.

[12] M.A. Johnson, "Impacts on Agriculture of Deregulating the Transportation System: Reply," *American Journal of Agricultural Economics*, vol. 65 (1983), p. 190.

[13] W W Wilson, "Modal Shares, Car Shortages, and Multiple-car Rates in Grain Transportation," *North Central Journal of Agricultural Economics* (Fargo, ND: North Dakota State University, July 1984), vol. 6, no. 2, p. 68.

[14] Wilson, p. 62.

[15] Ghulum Sarwar and Dale G. Anderson, (1989), p. 890.

The improved financial performance of railroads throughout the 1980's attests to the success of Staggers. Despite this success, the increased rate flexibility allowed under Staggers has proven insufficient to prevent railcar shortages for grain shippers. The recurring problems of railcar supply that have affected grain shippers since the late 1980's can be explained in part by the increasing reliance of carriers and shippers on general tariff rate making.

Following passage of the Staggers Act, rail grain contracting increased rapidly in the early and mid-1980's before dropping sharply in 1987. During the 1980–83 period, grain contracting activity averaged only 448 contracts per year. Contract activity increased rapidly in the mid-1980's to 2,770 contracts in 1985 and 2,935 contracts in 1986.[16] Rail grain contracts then fell off sharply.[17] By 1988, the number of rail grain contracts had fallen by more than 40 percent to only 1,625 contracts that year.[18,19] This decrease has been attributed to changes in the contract disclosure rules for grain implemented by the Interstate Commerce Commission (ICC) in January 1987 and to major shifts in the commercial policies and strategies of rail carriers.[20,21]

Estimates indicate that the amount of rail grain shipped under contract dropped from 63 percent in 1986 to 40 percent in 1988.[22] The decreasing use of contracts has resulted in a shift back to general tariff pricing for grain shipped by rail. With greater reliance on general tariffs to price freight service, rail carriers are less able to respond to sudden changes in market conditions.

The regulation of general tariff rates creates an inherent lack of flexibility in rail grain rates. For rail carriers, rate increases cannot become effective until 20 days after notice is published. Rate decreases cannot become effective until 10 days after notice is published.[23] In addition to the regulatory requirements under which rail rates can be adjusted, there are administrative considerations that affect the ability and willingness of carriers to change rates. Frequent general tariff rate adjustments raise administrative costs for carriers. Although improved under Staggers, general tariff rate-making practices make the pricing of rail transportation service much less flexible than the pricing of grain.

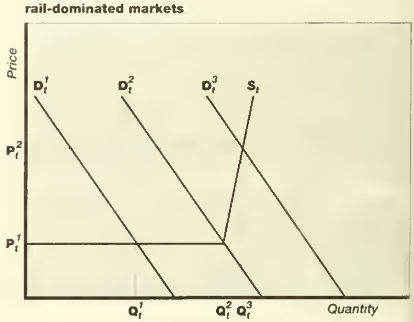
Sudden changes in grain supply and demand can change the quantities of grain shipped significantly without affecting the rail rate for such shipments. When the demand for rail transportation exceeds supply, grain shippers experience shortages of railcars. Although shortages may not affect rail rates in the short run, they do affect transfer costs. Changes in transfer costs quickly affect grain prices by changing the relationship that exists between country and terminal market prices.

Figure 2 illustrates the short-run relationship that exists between the supply and demand for grain transportation in rail-dominated markets when rail rates are unresponsive to demand. With a fixed supply of rail transportation offered at a fixed rate, price remains constant at Pt^1 from quantity zero through Qt^2. As the demand for transportation shifts from Dt^1 to Dt^2, as the result of increased demand for grain, quantity increases from Qt^1 to Qt^2. Beyond point Qt^2, the supply schedule for transportation (*St*) bends sharply upward such that an outward shift in demand to Dt^3 results in an increase in quantity to Qt^3 and an increase in price to Pt^2.

Under the assumption of short-run rail rate inflexibility, the price spreads between terminal and country markets served predominantly by rail should correspond to the depiction of transportation supply shown in figure 2. The supply curve for transportation in rail-dominated markets would be perfectly elastic up to the point where short-run rail capacity offered under general tariff rates is exhausted. At that point, transportation supply suddenly becomes highly inelastic. The bent supply curve is explained by the short-run inflexibility of general tariff rates and rail capacity. In rail-dominated markets, the prevailing rail rate represents the least-cost transportation alternative and, thus, establishes the floor price for transportation. This floor price prevails at all quantities below the short-run maximum capacity that carriers will offer under general tariff rates. Once the short-run quantity of rail capacity available under general tariff rates is exhausted, additional transportation capacity must be supplied through negotiated rail contract or premium service agreements, or by alternative transportation modes. All of these alternatives provide only marginal increases in capacity and only at significantly higher prices.

In markets where transportation rates and supply respond quickly to changes in demand, marketing margins mirror changes in transportation costs. In markets where transportation rates are relatively inflexible and demand frequently exceeds supply at the prevailing rate, marketing margins

Figure 2
Grain transportation supply and demand in rail-dominated markets



[16] S. Fuller, F.J. Ruppel, and D.A. Bessler, "Effect of Contract Disclosure on Price: Railroad Grain Contracting in the Plains," *Western Journal of Agricultural Economics*, vol. 15, no. 2 (1990), pp. 265–271.

[17] Transmode Consultants, Inc., *Effects of Disclosure Requirements on Railroad Grain Transportation Contracts*, (Washington, DC: U.S. Department of Transportation, Federal Railroad Administration, Office of Policy, FRA-RRP-92-01, 1992), p. 45.

[18] Association of American Railroads, *The Grain Book*, 1987/88 (Washington DC: AAR, Information and Public Affairs Department, 1988), p. 2.

[19] Fuller, Ruppel, and Bessler, pp. 265–271.

[20] Association of American Railroads, "Grain Contracts Drop With More Disclosure," *On Track* (Washington, DC: AAR, Information and Public Affairs Department, April 1988), vol. II, no. 7, pp. 1–3.

[21] Transmode Consultants, Inc., p. 45.

[22] Fuller, Ruppel, and Bessler, pp. 265–271.

[23] 49 U.S.C. § 10762(c).

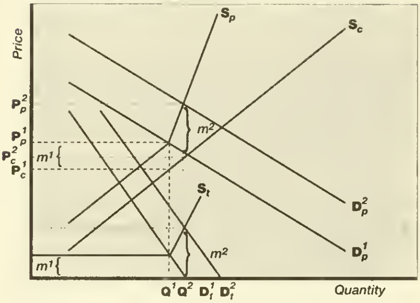
adjust in response to the availability of transportation. Constraints on transportation capacity cause grain elevator managers and merchants to increase their margins to cover the increased cost of alternative transportation and to offset the higher risks associated with increased supply uncertainty.

Volatility in farm prices can be attributed to volatility in the marketing margins for grain. Johnson suggested that, prior to Staggers, the volatility in farm prices was the result of uncertainty in transportation availability. Following Staggers, he believed that such volatility would be, at least in part, a function of transportation price uncertainty.[24] Uncertainty in the level of price spreads between country and terminal markets continues to exist, whether because of transportation availability or rate uncertainty.

Tight supplies of railcars increase price spreads or marketing margins, thus reducing country prices relative to terminal market prices. Testimony before the ICC in Ex Parte No. 490, *Grain Car Supply—Conference of Interested Parties* supports the fact that price spreads between terminal and country markets respond to the availability of rail transportation.[25] Elevator managers from North Dakota reported that during the fall and winter of the 1989/90 marketing year they reduced their cash grain bids to farmers in response to shortages of railcars.[26] Wheat producers testified that when no viable alternative transportation exists, shortages of railcars cause basis relationships to widen, and local cash prices to fall.[27] In both cases, these observations were associated with significant shifts in the demand for grain in export or terminal markets.

Figure 3 provides a model to assess shifts in export demand and accompanying price adjustments when the supply of transportation is consistent with the bent supply curve in figure 2. Figure 3, like figure 1, conceptualizes the classic derived demand model under which grain price spreads are determined. The supply schedule for grain in the country is represented by Sc, and the initial demand schedule for grain at the port is represented by Dp^1. As a simplification for the depicted model, the supply and demand for transfer services is assumed to reflect only transportation; all other costs associated with transfer are assumed to be zero. The initial

Figure 3
Grain price spreads between the country and export position in rail-dominated markets with an outward shift in demand



demand for transportation is derived from the interaction between the Sc and the Dp^1 schedules and is shown as Dt^1. The supply of transportation is given by the market and shown as the bent curve St. The intersection of Dt^1 and St determines the equilibrium quantity of transportation and grain (Q^1); the price of transportation or margin (m^1); the price of grain in the country (Pc^1); and the price of grain at the port (Pp^1). The price spread between the country and port is Pp^1–Pc^1 and is equal to m^1 given the simplifying assumption that transportation represents the only good or service required to transfer grain.

Figure 3 also illustrates changes that would occur in the market as a result of an increase in export grain demand. With increased export demand, the demand for grain at the port shifts outward to Dp^2, while supply at the country remains at Sc. The new demand schedule for transportation, derived from Sc and Dp^1, is thus Dt^2. The supply of transportation remains at St with a new equilibrium quantity of grain and transportation (Q^2), and a new price of transportation or margin (m^2). The new price spread between the country and port is Pp^2–Pc^2 and equal to m^2. The kinked supply schedule for grain at the port is shown as Sp and reflects the kinked nature of the supply schedule for transportation (St). Consistent with the inelastic nature of the upward portion of the Sp curve, beyond Q^1, increases in demand result in increases in price at the port that are large relative to the change in quantity. The increase in price at the port (Pp^2–Pp^1) is also large relative to the increase in price at the country (Pc^2–Pc^1).

[24] Johnson, p. 190.

[25] Interstate Commerce Commission, Ex Parte No. 490, *Grain Car Supply—Conference of Interested Parties* (Washington DC: ICC, September 18, 1990).

[26] Testimony of Jarvis Haugeberg, manager, Farmers' Association of Church's Ferry, *Grain Car Supply—Conference of Interested Parties*, Ex Parte No. 490, official transcript, (Washington DC: Interstate Commerce Commission, September 18, 1990), p. 43.

[27] Testimony of James Pelton, Chairman of Transportation Committee, National Association of Wheat Growers, *Grain Car Supply—Conference of Interested Parties*, Ex Parte No. 490, official transcript, (Washington DC: Interstate Commerce Commission, September 18, 1990), p. 141.

Modeling the Empirical Impact of Railcar Supply on Price Spreads

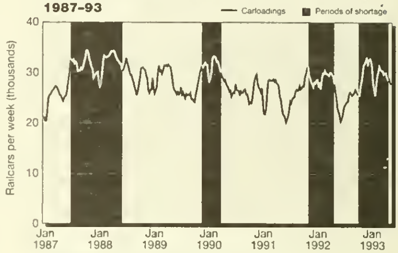
A variety of factors affect the relationship between grain prices in terminal markets and the prices that simultaneously exist in local or country markets. Fuller et al. modelled these factors to assess the impact rail deregulation had upon rates in the Plains and Corn Belt regions.

Fuller et al. attempted to measure rail rate changes through adjustments in spatial price spreads. In order to isolate the impact of deregulation, they controlled for changes in export demand, local supply, storage, and marketing services. They also attempted to control for changes in transportation costs to isolate the real rate changes.[28] Implicit in their analysis is the assumption that rail supply was relatively unconstrained. An important implication of this assumption is that rail rates were flexible enough to achieve market-clearing levels such that all demand is supplied at the prevailing market price. In the early to mid-1980's the assumption was valid, given the level of discounting that occurred under confidential contracts and the prevalence of railcar surpluses. In more recent years as surpluses have been reduced and supply and demand for railcars has come more into balance, the assumption no longer reflects the realities of the market.

Since 1987, steady domestic demand and increased world demand for U.S. grain has resulted in four distinct periods of railcar shortages. The first period began in June 1987 and did not completely abate until May 1988. The nature of this extended shortage was discussed by Klindworth and Norton.[29] The second shortage followed the fall 1989 harvest, beginning in November and easing the following March. During both the 1991/92 and 1992/93 harvest periods, grain shippers again experienced railcar shortages. In both years, the problems began in October during the fall harvest and continued through April of the following year. Figure 4 shows these periods in reference to a 4-week moving average for U.S. grain carloadings. All four shortages coincided with periods when weekly grain carloadings exceeded 30,000. Figure 4 also illustrates, that the U.S. grain industry experienced railcar supply problems nearly one-third of the time between January 1987 and April 1993.

The occurrence of these shortage periods contradicts past conjecture that increased rate flexibility under Staggers would provide for supply and demand balances in the market for rail grain transportation. The recurrence of railcar shortages suggests that post-Staggers rate adjustments, alone, are insufficient to balance supply and demand or provide the necessary market incentives to add capacity to the existing fleet. In the absence of short-run capacity or rate adjustments, grain price spreads between terminal and country markets fluctuate to offset imbalances in railcar supply and demand. During periods of high demand, price spreads increase beyond the normal cost of transfer, reflecting the constrained nature of railcar supply. This price spread response is consistent with theory and the real-market observations of grain shippers. Demonstrating it empirically provides a basis from which to assess the economic impact of railcar shortages on U.S. grain markets.

Figure 4
Rail carloadings of grain and periods of shortage, 1987-93



Sources Association of American Railroads, *Weekly Railroad Traffic*
U.S. Department of Agriculture, Agricultural Marketing Service, *Grain Transportation Report*
Note Carloadings are shown as 4-week moving averages

Defining the Statistical Model

The model defined in this analysis includes, by necessity, a variable that identifies the level of railcar surplus or shortage. The model also has to control for several other factors that could affect the terminal-to-country price relationship.

Consistent with the Fuller et al. study, the model includes variables that control for shifts in export demand and local supply.[30] It also includes a variable to control for shifts in the demand for rail grain transportation. Unlike the Fuller et al. model, which attempted to explain changes in rail rate levels and thus had rail rates as the dependent variable, this model includes rail rates as an independent variable. Most importantly, the model includes an independent variable for railcar availability.

The general regression model for this analysis is defined as follows:

$$\begin{aligned} SPREAD_m = {} & B_0 + B_1EX_m + B_2LS_m + B_3TBILLS_m \\ & + B_4RR_m + B_5RV_m + B_6RA_m \\ & + \text{(binary variables for selected origin State)} \\ & + \text{(binary variable for commodity)} \\ & + \text{(binary variables for season)} \\ & + U \end{aligned}$$

[28] Fuller, MacDonald, Bessler, and Wohlgenant, p. 3.

[29] Keith A. Klindworth and Jerry D Norton, Railcar Shortages for Grain Shippers: *A Current Overview* (Washington, DC: U.S. Department of Agriculture, Office of Transportation, April 1988). .

[30] Fuller, MacDonald, Bessler, and Wohlgenant, pp. 4–5.

where: **SPREAD** = terminal price less country price
EX = volume of grain exported
LS = supply of grain
TBILLS = interest rate on 3-month U.S. Treasury Bills
RR = rail rate
RV = volume of grain railed
RA = railcar availability
U = unexplained residuals

and: m denotes a specific market defined by origin State and destination port region

Shipment origin-destination pairs are defined to identify specific markets (m's). These were selected subject to the constraints of available data and the need to limit the scope of the analysis to markets where rail is the dominant mode of grain transportation. To account for the pooling of time-series and cross-section data, a least squares *dummy variables* model is used to provide consistent least squares estimators of the coefficients (B_i's). This commonly used adaptation of the *covariance model* replaces the constant or intercept term with the binary or "dummy" variable for the first cross-sectional group and includes additional binary variables for each of the remaining groups.[31] Binary variables are also included to account for commodities and seasons.

Selecting Commodities and Markets

Wheat and corn were selected for this analysis because their transport accounts for more than two-thirds of all U.S. grain transportation demand. During the 1980's, shipments of corn and wheat accounted for 47 and 24 percent, respectively, of all U.S. grain movements. Together corn and wheat accounted for 75 percent of all U.S. grain exports.[32]

Terminal markets selected are restricted to regional port areas where grain movements and prices are much more easily identified and segregated. The list of terminal markets is further limited to the Texas Gulf and the Pacific Northwest because these two regions represent the most significant U.S. ports that are served predominately by rail.

Table 1 provides U.S. grain export inspections for the country's major port regions for 1986 through 1989. During the 1986–89 period, Texas Gulf ports accounted for 37 percent of all wheat exported and Pacific Northwest ports accounted for 32 percent. Although the Pacific Northwest accounted for only 20 percent of all U.S. corn exports, it is clearly the second largest port for corn exports.

Table 2 shows that Texas Gulf ports receive 91 percent of their grain by rail, and Pacific Northwest ports receive 67 percent by rail. For corn delivered to the Pacific Northwest and for wheat to the Texas Gulf, these percentages are even higher. Ninety-five percent of all wheat delivered to the Texas Gulf arrives by rail. For all corn delivered to the Pacific Northwest, 94 percent arrives by rail. Despite the importance of barge transportation, 46 percent of all wheat exported from the Pacific Northwest arrives at port by rail.

The selection of origination markets is based on several criteria. First and foremost is the need to identify those origination markets that move grain into the Texas Gulf and Pacific Northwest ports. Price spreads between markets are only relevant to the costs of transfer in markets that trade. For price spreads to be related to the supply and demand of rail-

Table 1—U.S. grain export inspections by year and region

Year and Region	Wheat	Corn	Other	Total
		—1,000 bushels—		
1986				
Lakes & Seaway	82,734	34,578	77,157	194,469
Atlantic	26,986	81,711	59,366	168,063
River and East Gulf	164,888	764,248	736,746	1,665,882
Texas Gulf	321,882	18,069	56,975	396,926
Pacific Northwest	312,132	151,133	88,679	551,944
Other	3,109	21,219	31,060	55,388
Total	911,731	1,070,958	1,049,983	3,032,672
1987				
Lakes & Seaway	60,074	73,028	71,471	204,573
Atlantic	23,441	84,007	25,244	132,692
River and East Gulf	188,839	1,167,601	775,379	2,131,819
Texas Gulf	495,562	16,363	84,710	596,635
Pacific Northwest	355,715	257,372	138,852	751,939
Other	16,774	36,644	45,110	98,528
Total	1,140,405	1,635,015	1,140,766	3,916,186
1988				
Lakes & Seaway	63,859	83,840	55,829	203,528
Atlantic	40,428	67,487	30,970	138,885
River and East Gulf	276,079	1,217,948	645,689	2,139,716
Texas Gulf	618,583	21,937	133,145	773,665
Pacific Northwest	513,986	412,133	84,859	1,010,978
Other	26,437	42,572	63,539	132,548
Total	1,539,372	1,845,917	1,014,031	4,399,320
1989				
Lakes & Seaway	78,608	77,025	67,842	223,475
Atlantic	88,636	95,479	45,438	229,553
River and East Gulf	416,855	1,447,845	523,122	2,387,822
Texas Gulf	395,497	48,221	132,040	575,758
Pacific Northwest	388,255	514,827	121,949	1,025,031
Other	2,029	22,870	69,807	94,706
Total	1,369,880	2,206,267	960,198	4,536,345

Source U S Department of Agriculture, Federal Grain Inspection Service

Table 2—Rail shares of U.S. wheat and corn exports, by port, 1984-87 weighted averages

Region	Wheat	Corn	All Grains
		—percent—	
Lakes	66	12	38
Atlantic	78	100	93
East Gulf	11	91	68
River Gulf	10	8	7
Texas Gulf	95	84	91
Pacific	46	94	67
Mexico/Land	100	100	100
All	60	38	42

Source *Railcars for Grain: Future Need and Availability*, 1989

[31] Jan Kmenta, *Elements of Econometrics*, 2nd ed. (New York: Macmillan Publishing Company, 1986), pp. 630–631.

[32] Jerry D. Norton, Paul J. Bertels, and Freeman K. Buxton, Transportation of U.S. Grains: *A Modal Share Analysis* (Washington, DC: U.S. Department of Agriculture, Agricultural Marketing Service, July 1992), p. 6.

Table 3—Production for the top 14 wheat-producing States, 1986–89

State	1986	1987	1988	1989	Percent of total for 1986–89 period
		—1,000 bushels—			
Kansas	336,600	366,300	323,000	213,600	15.4
North Dakota	292,320	269,120	103,390	242,320	11.3
Oklahoma	150,800	129,600	172,800	153,900	7.5
Montana	138,520	151,220	59,970	145,030	6.1
Washington	116,850	114,285	124,620	110,610	5.8
Texas	120,000	100,800	89,600	60,000	4.6
Minnesota	103,666	102,588	51,730	102,504	4.5
South Dakota	108,660	106,704	38,006	83,080	4.2
Colorado	96,430	97,380	79,540	62,100	4.2
Idaho	81,750	85,500	75,520	91,420	4.2
Nebraska	76,000	85,800	72,000	55,350	3.6
Illinois	36,080	56,050	67,500	105,020	3.3
Missouri	18,810	35,420	75,950	86,950	2.7
Oregon	58,405	52,920	51,800	53,835	2.7
Other	356,744	353,793	426,775	470,099	20.0
U.S.	2,091,635	2,107,480	1,812,201	2,035,818	100.0

Source: U.S. Department of Agriculture, National Agricultural Statistics Service.

cars, it is essential that the markets selected for study are actively linked by rail transportation.

Originating country markets were identified at the State level. Originating States were selected from the most important corn- and wheat-producing regions. Table 3 lists the 14 top wheat-producing States in the United States for the 1986–89 period. These States accounted for 80 percent of all U.S. wheat production during the 4-year period. Table 4 lists the 9 top corn-producing States. These States accounted for nearly 80 percent of all U.S. corn production during this period.

Rail-dominant origin States were then selected from these States. Of the top 14 wheat-producing States (table 5), only Washington, Illinois, Missouri, and Oregon ship substantially less than 50 percent of their interstate wheat by rail. Of the corn-producing States (table 6), only Illinois, Wisconsin, and Missouri ship less than one-half of their interstate corn by rail. The availability of barge transportation in these States reduces their dependence upon rail.

Beyond identification of those States that rely heavily upon rail transportation to ship grains, it is also critical to define actual rail markets for wheat exported from the Texas Gulf and wheat and corn exported from the Pacific Northwest. This is done by determining which States actively ship grain into the Texas Gulf and Pacific Northwest markets.

Table 7 provides data on 1985 wheat shipments from the top 14 wheat-producing States to the Pacific Northwest and Texas Gulf export markets. Table 7 identifies the total volume shipped for each State and the rail volume shipped to each port region. In 1985, Montana, Washington, Idaho, and Oregon shipped 46.2, 37.9, 43.1, and 28.4 percent, respectively, of their wheat to the Pacific Northwest market by rail. Although a significantly smaller proportion of its wheat was shipped into the Pacific Northwest market, North Dakota was also selected as an origination market for export grain at this port region because of the State's geographic and production characteristics. In 1985, Kansas, Oklahoma, and Texas shipped 24.0, 46.5, and 37.7 percent, respectively, of their total wheat shipments into the Texas Gulf export market by rail. Despite the 1985 data given in table 7, country markets in Colorado and Nebraska were assumed to be much more closely tied to the Texas Gulf market because of these States' production characteristics and information from the *Carload Waybill Sample*.[33] Together, the 10 selected States accounted for 65 percent of all U.S. wheat production during the 1986–89 period.

Table 8 provides data on 1985 corn shipments from the top 9 corn-producing States to the Pacific Northwest export market. As the data indicate, only Minnesota, Nebraska, and South Dakota ship a significant portion of their corn by rail into the Pacific Northwest ports. In terms of production, these three States accounted for 24 percent of all U.S. corn production during the 1986–89 period. The selected origination States are shown for both corn and wheat in figure 5.

Describing Variables and Data Sources

The model incorporates variables that economic theory suggests should explain changes in the country-to-terminal market price spreads. The actual relationship is estimated using statistical procedures and secondary data. In addition to price series data necessary to calculate price spreads, secondary data is used to account for changes in rail rates and the supply and demand conditions for grain and rail transportation. Time-series data were selected for (1) country prices, (2) terminal prices, (3) elevator margins, (4) rail rates, (5) export volumes, (6) local grain supply, (7) export rail volume, and (8) railcar availability.

Price Spreads

One approach frequently used to determine grain prices at the farm is to use country elevator bid prices. Country elevator

[33] Interstate Commerce Commission, *Carload Waybill Sample* (Washington, DC: ICC, Office of Economics).

Table 4—Production for the top 9 corn-producing States, 1986–89

State	1986	1987	1988	1989	Percent of total for 1986–89 period
		—1,000 bushels—			
Iowa	1,626,750	1,306,500	898,800	1,445,500	19.0
Illinois	1,404,000	1,201,200	700,800	1,322,250	16.7
Nebraska	896,000	812,200	818,400	852,000	12.2
Indiana	695,400	631,800	415,000	691,600	8.8
Minnesota	707,600	635,000	347,800	700,000	8.6
Ohio	476,160	362,400	255,000	342,200	5.2
Wisconsin	365,800	330,400	130,650	310,800	4.1
Missouri	280,720	242,950	153,520	219,840	3.2
South Dakota	233,700	228,250	132,000	190,800	2.8
Other	1,563,734	1,321,373	1,076,711	1,452,162	19.5
U.S.	8,249,864	7,072,073	4,928,681	7,527,152	100.0

Source: U.S. Department of Agriculture, National Agricultural Statistics Service.

Table 5—Rail shares of wheat shipments for the top 14 wheat-producing States, 1985

State	Shipment type: Interstate	Intrastate	All
	—percent—		
Kansas	86.7	28.7	46.7
North Dakota	73.5	3.8	41.3
Oklahoma	78.8	100.0	83.6
Montana	76.2	100.0	76.5
Washington	30.6	19.1	24.2
Texas	80.7	18.3	37.0
Minnesota	46.6	14.6	30.9
South Dakota	72.5	0.2	36.6
Colorado	59.2	6.8	36.9
Idaho	56.6	1.3	32.6
Nebraska	82.2	8.0	27.8
Illinois	42.6	4 5	21.2
Missouri	33.1	13.3	23.1
Oregon	29.2	100 0	29.5

Source *Wheat Movements in the United States*, 1985

Table 6—Rail shares of corn shipments for the top 9 corn-producing States, 1985

State	Shipment type: Interstate	Intrastate	All
	—percent—		
Iowa	49 6	25.8	37.0
Illinois	22.2	14.1	18.6
Nebraska	68.8	4 6	50.8
Indiana	62.1	59.7	60.8
Minnesota	50.2	24.7	42.0
Ohio	59.2	19.9	48.6
Wisconsin	12.9	8.3	11.9
Missouri	25.2	11.6	23.9
South Dakota	69.2	0.0	50.8

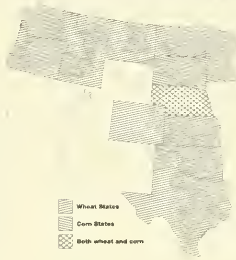
Source *Corn Movements in the United States*, 1985.

Table 7—Shipments of wheat to Pacific Northwest and Texas Gulf ports from the top 14 wheat-producing States, 1985

State	Total volume shipped	Pacific Northwest: Rail volume shipped	Pacific Northwest: Percent of total shipped	Texas Gulf: Rail volume shipped	Texas Gulf: Percent of total shipped
	1,000 bushels	1,000 bushels		1,000 bushels	
Kansas	516,331	3,698	0.7	124,050	24.0
North Dakota	237,600	20,606	8.7	2,780	1.2
Oklahoma	146,355	0	0.0	68,033	46.5
Montana	77,700	35,918	46.2	0	0.0
Washington	119,116	45,178	37.9	0	0.0
Texas	202,459	0	0.0	76,388	37.7
Minnesota	230,633	1,793	0.8	0	0.0
South Dakota	104,763	0	0.0	467	0.4
Colorado	121,399	21,021	17.3	3,878	3.2
Idaho	56,698	24,462	43.1	0	0.0
Nebraska	109,230	9,918	9.1	6,292	5 8
Illinois	88,507	0	0.0	0	0 0
Missouri	66,215	392	0.6	6,668	10.1
Oregon	35,777	10,176	28.4	0	0.0

Source *Wheat Movements in the United States*, 1985

Figure 5
Wheat- and corn-producing States selected for the model



bids closely approximate prices received by farmers for cash grain, but bids may also have bias. For example, decreased farm sales should exert upward pressure on country prices resulting in lower sales volumes during periods of the higher prices. Conversely, increased farm sales should exert downward pressure on country prices, resulting in larger sales volumes during periods of lower prices. Using cash grain bids may also result in regional biases because of the elevators selected for survey. In an effort to overcome these potentials for bias, this analysis uses USDA "Prices Received by Producers" data.[34] This price series reflects a true mean farm price because it is the total cash receipts of producers divided by the quantity sold. However, because this data is reported monthly by State it constrains the analysis to monthly observations, and the origination market specification to the State level.

Terminal market prices used were reported by the USDA "Monthly Average Cash Grain Bids" in *Grain and Feed Market News*.[35] Monthly average corn prices for the Pacific Northwest are not given by this report, but were provided by the USDA, Agricultural Marketing Service, Livestock & Seed Division. The corn price spreads are based on the Pacific Northwest cash price for No. 2 Yellow Corn. The Texas Gulf wheat price is for No. 1 Hard Winter, ordinary protein at Houston, TX. The Pacific Northwest prices used are for No. 1 Dark Spring, 14 percent protein, and No. 1 Soft White at Portland, OR.

Calculations of each State's country-to-terminal price spreads for wheat are made based on the most appropriate wheat classification as determined by production. Table 9 provides wheat production by classes in 1989 for each of the 10 selected wheat States. Table 10 provides the same information in terms of percentages of each State's total wheat production. For the States of Kansas, Oklahoma, Texas, Colorado, and Nebraska, which ship wheat into the Texas Gulf market, wheat production is primarily Hard Red Winter. Wheat classes vary significantly for those States shipping grain into the Pacific Northwest markets. Virtually all North Dakota wheat is spring wheat, predominantly Hard Red

[34] U.S. Department of Agricultural, *Agricultural Prices* (Washington DC: USDA, National Agricultural Statistics Service), various issues, 1986-90.

[35] U.S. Department of Agricultural, *Grain and Feed Market News* (Washington DC. USDA, Agricultural Marketing Service, Livestock & Seed Division), various issues, 1986–90.

Spring. Montana, Washington, and Idaho produce significant amounts of winter and spring wheats. Montana wheat is typically Hard Red. Washington and Idaho produce mostly Soft White varieties. Oregon, by contrast, produces virtually all Soft White wheat, and almost all is winter wheat.

Price spreads are calculated by subtracting each State's producer price from the terminal price for the type and class of grain identified as most representative of that State's production. The resulting spreads are shown conceptually in figures 1 and 3 as the country-to-port margins (m^n). Figure 6 shows the average monthly price spread taken over all markets and all observations during the 1986–89 study period.

Elevator Handling Margins

Given earlier assumptions about the competitiveness of grain merchandising and handling, it is assumed that the prices for these services were at their marginal costs. Since the most significant portion of the cost of holding grain is the interest cost on the cash value of that grain, the monthly yield on new issue 3-month U.S. Treasury Bills is used to track changes in the cost of grain handling and, thus, elevator margins.[16] These yields are shown for the 1986–89 period in figure 7.

Rail Rates

Since transportation costs typically represent the largest share of transfer costs between markets, the price of rail transportation is a critical variable in the model. Revenue information from the *Carload Waybill Sample* is used to estimate the price or rate for rail transportation.

Monthly average rail rates for each commodity and market are calculated as the weighted average rate for all observed shipments of that commodity in that market. For example, monthly rail rates for Nebraska corn are taken from those observed shipments of corn that originated in Nebraska and terminated in port areas of the Pacific Northwest. The rate (in cents per bushel) is calculated for each observed shipment during each month, then weighted by the shipment volumes to arrive at a monthly average rate. The monthly average rail rate for corn and wheat shown in figure 8 is the simple mean of the weighted average rates for the study markets.

The use of *Carload Waybill Sample* revenue data as an estimate of rates is sometimes questioned by individuals with a familiarity of the process used to report the revenue data. The arguments against using this revenue information are typically based on the belief that rates calculated from this data are substantially overstated for shipments made under contract. Railroads can and do mask the contract rates they report. Rail contracts may also include penalties or rebates based on performance over the life of the contract.[17] The penalties or rebates may not be reflected in the revenue reported on the waybill at the time of shipment. In some instances this may overstate rates; however, in the aggregate the *Carload Waybill Sample* revenue data has been shown to be reliable.

MacDonald used the 1983 *Carload Waybill Sample* to determine if the revenues reported from waybills included discounts offered under contract. He found that revenues for 25 heavily traveled routes were 22 percent below those that would have resulted under existing tariff rates. He also compared average revenue per ton for Class I railroads using the *Carload Waybill Sample* and the ICC's *Freight Commodity Statistics*. He found that both sources gave approximately the same measures of average revenues per ton for corn, soybean,

[16] U.S. Department of Commerce, *Survey of Current Business* (Washington DC: Commerce, Bureau of Economic Analysis), 1986–89.

[17] Klindworth, Sorenson, Babcock, and Chow, p. 15.

Table 8—Shipments of corn to Pacific Northwest ports for the top 9 corn-producing States, 1985

State	Total volume shipped	Rail volume shipped to PNW ports	Percent of total shipped
	—1,000 bushels—		
Iowa	789,272	25,851	3.3
Illinois	1,202,058	0	0.0
Nebraska	620,917	130,303	21.0
Indiana	881,279	0	0.0
Minnesota	452,481	56,071	12.4
Ohio	380,912	0	0.0
Wisconsin	85,932	0	0.0
Missouri	159,509	0	0.0
South Dakota	112,737	45,060	40.0

Source: *Corn Movements in the United States*, 1985.

Table 9—Wheat production for selected States by classes, 1989

	Winter			Spring		
State	Hard Red	Soft Red	White	Hard Red	White	Durum
	—1,000 bushels—			—1,000 bushels—		
Kansas	211,464	2,136	0	0	0	0
North Dakota	2,320	0	0	174,000	0	66,000
Oklahoma	153,900	0	0	0	0	0
Montana	54,000	0	0	85,000	0	6,030
Washington	6,890	0	62,010	10,428	31,283	0
Texas	56,400	3,600	0	0	0	0
Colorado	57,200	0	0	4,116	784	0
Idaho	9,639	0	47,061	15,624	19,096	0
Nebraska	55,350	0	0	0	0	0
Oregon	489	0	48,411	740	4,195	0

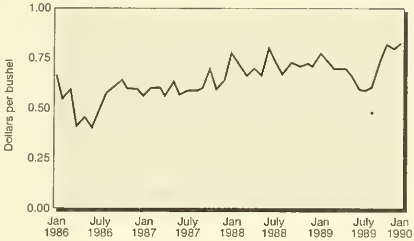
Source: U.S. Department of Agriculture, National Agricultural Statistics Service, *Crop Production*, 1989

Table 10—Wheat production for selected States, percent by classes, 1989

	Winter			Spring		
State	Hard Red	Soft Red	White	Hard Red	White	Durum
	—percent—			—percent—		
Kansas	99	1	0	0	0	0
North Dakota	1	0	0	72	0	27
Oklahoma	100	0	0	0	0	0
Montana	37	0	0	59	0	4
Washington	6	0	56	9	28	0
Texas	94	6	0	0	0	0
Colorado	92	0	0	7	1	0
Idaho	11	0	51	17	21	0
Nebraska	100	0	0	0	0	0
Oregon	1	0	90	1	8	0

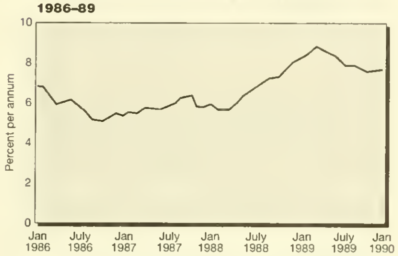
Source: U.S. Department of Agriculture, National Agricultural Statistics Service, *Crop Production*, 1989

Figure 6
Average monthly price spreads for study markets, 1986–89



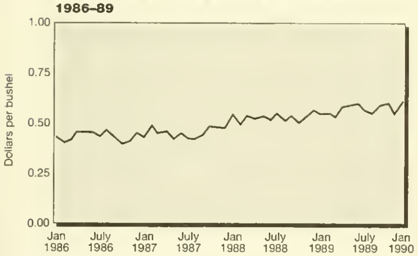
Source USDA, Agricultural Marketing Service

Figure 7
Monthly yield on 3-month U.S. Treasury Bills, 1986–89



Source U.S. Department of Commerce

Figure 8
Average rail rates for grain in study markets, 1986–89



Source Interstate Commerce Commission, *Carload Waybill Sample*

and wheat shipments.[38] Since all indications are that rail contracting has declined since the mid 1980's, MacDonald's findings seem valid for more recent *Carload Waybill Samples*, and they continue to support the appropriateness of this data as a source of rail rate information.

[38] James M. MacDonald, "Competition and Rail Rates for the Shipment of Corn, Soybeans, and Wheat," *Rand Journal of Economics*, vol. 18, no. 1 (1987), p. 154.

Grain Supply and Demand

Local supply and demand for grain affect price spreads between points in the marketing channel. Over time, price spreads should approximate transfer costs as arbitrage between the markets occurs. In the short run, however, geographically distinct markets may respond to variations in the local levels of grain supply and demand. As Hill and Davis showed, local supply and demand imbalances affect short-run price differentials.[39] Thus, changes in local supply and demand must be accounted for in any analysis of price spreads.

In export-driven markets, one easily identifiable factor affecting local supply and demand is export demand. In this study export grain volumes are used to measure shifts in demand for grain. Exports for the Texas Gulf and Pacific Northwest are taken from USDA Federal Grain Inspection Service export inspections.[40] Exports of Hard Red Winter wheat from the Texas Gulf are used for Kansas, Oklahoma, Texas, Colorado, and Nebraska. Exports of Hard Red Spring wheat from the Pacific Northwest are used for North Dakota. Combined exports of both Hard Red Spring and Hard Red Winter wheat from the Pacific Northwest are used for Montana. Soft White wheat exports from the Pacific Northwest are used for Washington, Idaho, and Oregon. For the selected corn States of Minnesota, Nebraska, and South Dakota, Pacific Northwest corn exports are used. These monthly exports are shown in figure 9.

Shifts in local supply were estimated from local wheat and corn stocks reported for each State by USDA's National Agricultural Statistics Service.[41] Stock levels during nonreported months are extrapolated from the reported data to approximate stock level changes. Figure 10 provides the aggregate wheat stocks for the 10 wheat States and the aggregate corn stocks for the 3 corn States in the study. As should be expected, these stocks reflect the cyclical nature of the production season for grain.

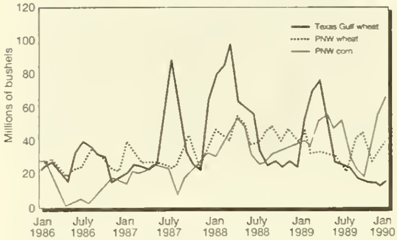
Several sources of grain demand exist at the local level. An accurate measure of this demand, however, is not available because data on grain disappearance is reported only at the national level. To estimate local demand, Fuller et al. calculated the ratio of unfilled storage capacity to total storage capacity for each originating State. Owners of grain storage capacity create demand for grain as they attempt to fill vacant facilities and generate storage income. This storage demand is an important part of local demand, but because storage capacity changes very little from month to month, the ratio of unfilled storage capacity to total storage capacity is highly and inversely correlated to the stock data. The addition of such a highly correlated variable adds little new information to the model, and greatly increases the potential for the type statistical problems associated with collinearity. For these reasons, no variable for local demand is used.

[39] Davis and Hill, pp. 135-136.

[40] U.S. Department of Agriculture, *Grain and Feed Market News*, 1986–90.

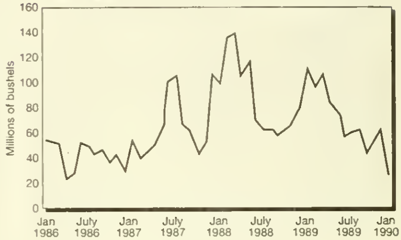
[41] U.S. Department of Agriculture, *Grain Stocks* (Washington DC: USDA, National Agricultural Statistics Service, Agricultural Statistics Board), various issues, 1986–90.

Figure 9
Corn and wheat exports from study ports, 1986–89



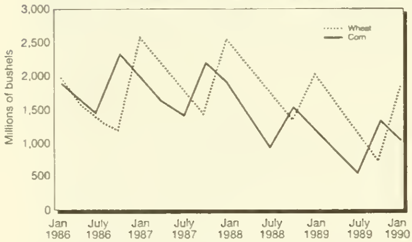
Source: USDA, Federal Grain Inspection Service
Note: Texas Gulf wheat includes Hard Red Winter and Hard Red Spring.
PNW wheat includes Hard Red Winter, Hard Red Spring, and White wheat.

Figure 11
Corn and wheat shipments by rail in study States, 1986–1989



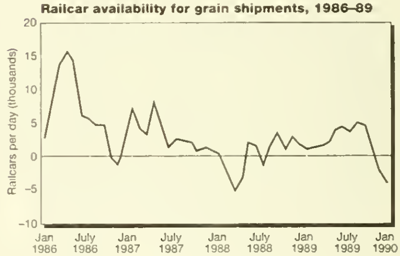
Source: Interstate Commerce Commission, *Carload Waybill Sample*

Figure 10
Corn and wheat stocks in study States, 1986–1989



Source: U.S. Department of Agriculture, National Agricultural Statistics Service

Figure 12
Railcar availability for grain shipments, 1986–89



Source: Association of American Railroads, *CS-44 Report*
Note: Railcar availability is defined as the number of jumbo covered hopper railcars in surplus less the number of cars ordered that cannot be supplied.

Rail Transportation Supply and Demand

The central hypothesis is that price spreads between country and terminal grain markets in rail-dominant corridors are affected by the availability of rail transportation. To test this hypothesis, it is essential that the model include variables that measure the supply and demand for rail grain transportation.

Within some range of quantity, even under an assumption of price inflexibility, increases in the rail transportation demand can be measured by the volume of grain moved by rail. The *Carload Waybill Sample* was used to determine the monthly volumes of corn or wheat shipped from each of the selected States to either the Pacific Northwest or Texas Gulf port regions. As an example, monthly grain shipment tonnages were determined for wheat shipped from Kansas to the Texas Gulf. In the case of Nebraska, the data set includes observations for monthly corn tonnages to the Pacific Northwest and monthly wheat tonnages to the Texas Gulf. The shipments of corn and wheat from the study States to the export ports are aggregated by month in figure 11.

Given the assumption of price inflexibility and the fixed nature of rail transportation supply in the short run, demand for rail grain transportation can exceed available supply. The occurrence of railcar shortages supports this and indicates that price adjustments alone are unable to equilibrate supply and demand in the market for rail grain transportation. One available measure of the imbalance in the market for rail grain transportation is the number of unfilled jumbo covered hopper railcar orders in relation to the number of surplus jumbo covered hopper railcars. The Association of American Railroads collected weekly data on the average surplus and unfilled orders for freight cars from 1979 through 1991. This data series reported these surpluses and unfilled orders by railroad and type of car as a daily average for each week.[42] An aggregate measure of railcar availability for grain shippers was calculated by subtracting the aggregate number of covered hopper railcars "on order and unfilled" on western U.S. railroads from the aggregate number of covered hopper railcars in surplus on western U.S. railroads. This aggregate measure of railcar availability is positive during surpluses and negative during shortages. Monthly averages are estimated from the reported daily averages by assigning each day the value reported that week, summing these for each month, then dividing by the total days in the month. Thus the railcar availability variable indicates the average daily number of

[42] Association of American Railroads, "Average Daily Freight Car Surpluses and Unfilled Orders, CS 44-C Report," (Washington, DC: Association of American Railroads, Transportation Division), 1986–89.

railcars in surplus or deficit on all western railroads during any given month. This variable is shown in figure 12.

Seasonality

Dummy, or binary, variables are included in the model to account for changes in marketing patterns throughout the year. Such patterns are typically influenced by weather. In some instances, seasonality is directly related to crop production. In other instances, it is tied to the effects of weather on transportation availability and capacity. To reflect the more obvious factors associated with seasonal changes, the months are grouped by quarter—the first quarter was March through May; the second quarter, June through August; the third quarter, September through November; and the fourth quarter, December through February.

Results of the Statistical Analysis

The regression coefficients and equation were estimated from the data already described. The variables included in the regression are defined in table 11. The entire raw data set includes 48 monthly observations for each of the 13 distinct markets as defined by origin State, destination port, and commodity. Combined, these observations totaled 624 cases for the 1986–89 period. In a limited number of cases, the *Carload Waybill Sample* failed to report any rail tonnages for a market during a particular month. In such instances, these cases were dropped from the data set because it was assumed that there was no active trade between these areas during those months. This assumption is supportable and convenient because, without actual shipments, there is no rate information available from the *Carload Waybill Sample*. Dropping these observations from the data set left 593 valid cases for analysis.

The results of the regression are provided in table 12. As indicated by the adjusted R-squared of 0.72, the variables included in the equation explained 72 percent of the variation in the price spread between the port and country prices. The F-statistic also indicates that the equation itself was significant at the .01 confidence level. Taken individually, the signs of the coefficients for each variable were consistent with what would be expected; however, not all variables were statistically significant at ordinary levels of confidence.

Table 11—Definitions of variables in the equation

Variable	Definition
Dependent variable:	
SPREAD	Monthly average per bushel export price for wheat and corn less the monthly average per bushel price received by producers for selected markets.
Independent variables:	
EX	Monthly export volumes of wheat and corn in thousand bushels for selected markets and classes.
LS	Monthly wheat and corn stocks in thousand bushels by selected States extrapolated between quarterly USDA stock reports.
TBILLS	Monthly average yield on new issue 3-month U.S. Treasury Bills.
RR	Monthly average rail rate for wheat and corn for shipments from selected States to export position in cents per bushel.
RV	Monthly volumes of wheat or corn shipped by rail from selected States to export position in thousand bushels.
RA	Monthly average number of jumbo covered hopper railcars in surplus less the number of such cars on order and unfilled per day on western U.S. railroads.
QONE	Dummy variable for seasonality for the March–May period
QTWO	Dummy variable for seasonality for the June–August period
QTHR	Dummy variable for seasonality for the September–November period. December–February was the omitted period.
CRN	Dummy variable used to account for differences between the wheat and corn markets. Corn was indicated by CRN = 1.
CO, ID, KS, MN, MT, NE, ND, OK, OR, TX, WA	Dummy variables for States as indicated by two-letter State postal codes. South Dakota was the omitted State

Quantitative Variables in the Equation

Coefficients were estimated for the quantitative variables included in the equation, and tested for their levels of statistical significance. The estimated coefficients provide information about the relationship between exports, local supplies, elevator handling costs, rail shipment volumes, rail

Table 12—Estimated coefficients, t-ratios, and elasticities for the equation

Variable	Coefficient	t-ratio	Elasticity***
(Constant)	.59966	9.943*	
EX	2.1576E-06	4.803*	.0867
LS	6.4404E-08	.966	.0250
TBILLS	.03004	5.078*	.3068
RV	1.4607E-06	1.094	.0122
RR	.09364	1.870**	.0720
RA	–6.7653E-06	–4.560*	–.0320
QONE	–.02154	–1.351	–.0083
QTWO	–.04159	–2.592*	–.0160
QTHR	.04228	2.693*	.0163
CRN	–.17858	–2.883*	–.0659
CO	–.20751	–3.347*	–.0223
ID	–.36570	–5.801*	–.0450
KS	–.25668	–3.252*	–.0316
MN	–.05578	–1.261	–.0069
MT	.05992	.874	.0074
NE	–.17816	–3.198*	–.0384
ND	.02292	.283	.0028
OK	–.24326	–3.668*	–.0299
OR	–.55826	–8.681*	–.0601
TX	–.20267	–2.871*	–.0249
WA	–.54653	–8.028*	–.0673

Adjusted R-squared .72094
Standard error .12860
N = 593
F = 73.82905*

Note * Indicates significantly different from zero at the .01 confidence level.
** Indicates significantly different from zero at the .10 confidence level
*** Indicates elasticity of price spread with respect to each variable calculated at the mean.

rates, railcar availability, and the spread between port and country prices.[43]

Exports

The coefficient on the level of exports (EX) proves to be highly significant in the model at the .01 confidence level. The positive sign of the coefficient indicates that as exports increase, the difference between the port and country price for grain increases, and, as exports decrease, the price difference decreases. As export demand increases, as indicated by increased exports, the port price increases relative to the country price to encourage grain to move from interior points to meet this increase in market demand. As export demand decreases, prices at the port decrease relative to prices in the country to provide a disincentive to move grain from the country to export positions.

Local Grain Supplies

As would also be expected, local grain supplies and price spreads are positively related, as indicated by the positive sign of the coefficient on the local supply variable (LS). However, the estimated coefficient is not found to be significant even at the .10 confidence level. All else considered, large local stocks of grain should place downward pressure on the country price relative to the port price, thus widening the spread between the two. As local supplies become more scarce, local demand should push country prices upward relative to export prices, and reduce the spread between them. Although the sign on the variable supports this relationship, the error associated with the coefficient results in the model's inability to establish this relationship at an acceptable level of statistical significance.

Elevator Handling Margins

The coefficient on the interest rate variable (TBILLS) used to explain changes in elevator handling margins, is positive in sign and highly significant in this model at the .01 confidence level. Increases in elevator handling costs widen the spread between country and port prices. To cover increased handling costs, country elevators increase margins by reducing bid prices and passing less of the port price back to the farmer. When handling costs decrease, margins decrease as elevators are able to offer higher bid prices for grain at interior points relative to prevailing port prices.

Rail Rates

The price of transportation, or rate, between two markets is positively related to the difference between the port and country prices for grain. The relationship proved to be significant in the model, but only at the .10 confidence level. The positive sign of the coefficient on the rate variable (RR) indicates that as rail rates rise, the price spread between the country and port increases. As rail rates fall, the spread decreases. If all else is held constant, country prices rise and fall relative to port prices in direct relation to the increase and decrease in rail rates.

Rail Shipment Volumes

Increased demand for rail transportation, as indicated by the volume of grain shipped by rail, is estimated to be positively related to changes in the price spread. The positive sign on the coefficient for rail volume (RV) suggests that as the volume of grain shipped increases, so will the difference between the port and country price. Although theory supports this relationship, the coefficient estimated for the variable did not prove to be statistically significant in this model.

Railcar Availability

The availability of railcars is found to be significant at the .01 confidence level, and inversely related to the spread between country and port prices. This finding supports anecdotal information already cited from grain shippers and producers. It is also consistent with the conceptual model of rail supply and demand described in figure 2, and the relationship depicted in figure 3 of country-to-port grain price spreads in markets dominated by rail transportation. The negative relationship between railcar availability and these price differences, as evidenced by the negative sign of the estimated coefficient, indicates that as the available supply of railcars decreases, the price for grain at the port increases relative to the price in the country.

This relationship can be explained by the market behavior of country elevator merchants. As export demand increases and railcars become increasingly less available for grain shipment, country merchants become increasingly less able to secure transportation to move grain to the export market. Lacking the ability to move grain out of country facilities, local elevators find it difficult to accept new grain delivered from the farm. To discourage farmers from making sales, country elevators must hold their bid prices low despite rising prices at the port. Country shippers may also be forced to seek higher priced transportation alternatives, if such alternatives exist. Shifts to alternative modes increase handling costs for local elevators. Given the cost structure for country elevator operations, increased handling and transportation costs must be passed on through wider margins between the prevailing port price and the bid price made to farmers.

The impact of changes in the availability of railcars varies greatly across regions. As railcar availability decreases, exporters are forced to source grain from regions more accessible by barge or truck. Grain prices in such regions typically carry a premium to those in more distant areas. Regional price differentials that normally exist are further exacerbated by reductions in the availability of railcars.

Binary Variables in the Equation

Qualitative information that is believed to affect country-to-port price spreads is included in the equation using binary

[43] The reader may note that exports, local supplies, elevator handling costs, rail shipment volumes, rail rates, and railcar availability may not only be related to price spreads, but may also be related to each other. Appendix A provides the correlation matrix for the data used in this model and a discussion of the correlation among these variables. The model was also estimated using lagged values for each of these variables. In all cases, the estimated equations resulted in marginally lower adjusted R-squared values and the coefficient on the lagged variables proved smaller and less significant that those on the non-lagged values.

variables to indicate seasons, crops, and States. Coefficients for these variables are estimated and tested for their levels of statistical significance.

Seasons

Signs and levels of statistical significance on the seasonal variables must be considered with respect to the December–February period. The estimated coefficient on the variable for the March–May period (QONE) is negative, suggesting that price spreads were smaller during the March–May period than in the December–February period. This relationship, however, fails to prove significant at ordinary levels of confidence. The coefficient on the variable for the June–August period (QTWO) is negative and significant at the .01 confidence level. This indicates that grain price spreads were smaller during the June–August period than during the December–February period. The coefficient on the variable for the September–November period (QTHR) is positive and significant at the .01 confidence level. Price spreads during this period were larger than during the December–February period. These findings are consistent with a seasonal pattern in which price spreads are greatest during the fall harvest and decrease throughout the post-harvest period.

Crops

A coefficient is estimated for the variable used to identify wheat and corn markets (CRN). The sign of this coefficient is negative and significant at the .01 confidence level. This indicates that the price spreads were smaller for corn than for wheat, at least within the parameters of the model. This seems logical, since corn is less susceptible than wheat to quality deterioration during handling and transportation.

States

Only the estimated coefficients on the variables for the States of Montana and North Dakota are positive in sign. Since South Dakota is the omitted State, this suggests that the price spreads in Montana and North Dakota are larger than those in South Dakota. The signs for the coefficients on the variables for all the other States are negative, indicating that the price spreads in these States are smaller than those in South Dakota. The coefficients estimated for Minnesota, North Dakota, and Montana are the only ones that prove insignificant at ordinary levels of confidence. The estimated coefficients for the other State variables are all significant at the .01 confidence level.

Estimated Price Spread Responses

The regression results indicate that railcar availability is a significant variable when explaining variations in the price spread for grain between export and country markets. The coefficients estimated by regression and the descriptive statistics calculated on the data set provide information about the responsiveness of the dependent variable--price spread--to changes in the independent variables of the model, particularly railcar availability.

Elasticities of Price Spread With Respect to Selected Model Variables

Using the mean values for the independent variables and their estimated coefficients, elasticities are calculated at the mean for the independent variables used in the model. These elasticities of price spread with respect to each variable are provided in table 12. The means, minimums, maximums, and standard deviations for selected variables used in the model are provided in table 13.

The elasticities of price spread with respect to the quantitative variables in the model are all found to be in the inelastic range. The variable used as a proxy for elevator margin (TBILLS) proves to be the most influential on price spread with an elasticity of .3068. Price spread proves to be less responsive to exports (EX) and rail rates (RR) with elasticities of .0867 and .0720, respectively. The elasticities of price spread with respect to the local supply (LS) and rail volume (RV) are calculated to be .0250 and .0122. Both, however, are statistically insignificant in the model. The elasticity of price spread with respect to railcar availability (RA) is calculated to be –.0320.

Price Spread Responses to Railcar Availability

The elasticity of price spread with respect to railcar availability indicates the percentage change in price spread that would result from a 1-percent change in the variable for railcar availability. This point elasticity, calculated at the mean, indicates that for every 1 percent change in railcar availability, price spread will change in the opposite direction by .0320 percent. Although small in absolute value, this elasticity underscores the impact of railcar supply on price spreads. As an example, the –.0320 elasticity suggests that the country-to-port price spread will increase or decrease by 1 cent per bushel for every change in railcar availability of 1,477 cars per day.

Estimated price spread responses to changes in the level of railcar availability are provided in table 14. Based on the –.0320 elasticity of price spread, the estimated values in table 14 indicate that at the railcar availability mean of 3072 cars per day, the point estimate for price spread from the model is 65 cents. Estimating price spread for railcar availability at 7,255 cars per day, one standard deviation above the mean, results in a price spread estimate of 62.2 cents. Estimating price spread for railcar availability at –1,111 cars per day, one standard deviation below the mean, results in a price spread of 67.8 cents. As an approximation of the impact of railcar availability on grain price spreads, a change in the

Table 13—Descriptive statistics for selected variables included in the regression equation

Variable	Mean	Minimum	Maximum	Standard deviation
SPREAD*	.65	–.04	1.63	24
EX**	26,125.53	.00	96,191.00	19,035.42
LS**	252,467.65	9,858.00	1,321,382.00	263,806.21
TBILLS***	6.64	5.18	8.83	1.07
RR*	.50	.04	1.79	.24
RV**	5,427.35	114.00	46,172.00	6,578.33
RA****	3,071.90	–5,287.00	16,244.00	4,182.81
N = 593				

Note * Cents per bushel
** Thousand bushels.
*** Annual percentage yield
**** Average daily number of railcars available

Table 14—Estimated price spread responses to changes in railcar availability

Railcar availability[1]	Estimated percentage change in price spread from the mean[2]	Estimated price spread[3]
—railcars per day—	—percent—	—cents per— bushel
–5,000	8.4	70.5
–4,000	7.4	69.8
–3,000	6.3	69.1
–2,000	5.3	68.4
–1,111*	4 4	67 8
–1,000	4.2	67.8
0	3.2	67.1
1,000	2.2	66.4
2,000	1 1	65.7
3,000	0.1	65 0
3,072**	0.0	65.0
4,000	–1.0	64 4
5,000	–2.0	63.7
6,000	–3.0	63.0
7,000	–4 1	62.3
7,255*	–4.4	62.2
8,000	–5.1	61.7
9,000	–6.2	61.0
10,000	–7.2	60.3

[1] "Railcar availability" is defined as the number of cars in surplus minus the number of cars ordered and unfilled on western railroads

[2] "Estimated percentage change in price spread from the mean" for each level of railcar availability based on the estimated elasticity of the price spread with respect to railcar availability calculated at the mean

[3] "Estimated price spread" equals the observed mean for price spread plus the "estimated percentage change in price spread."

*Indicates one standard deviation from the observed mean for railcar availability

**The observed mean for railcar availability

available supply of railcars of 8,366 cars per day (a range in which more than two-thirds of all observations fall) can affect price spreads by as much as 5.6 cents per bushel.

Since the point elasticity used for these estimates is taken at the mean, based on the parameters estimated from the model, estimating changes in price spread based on this value must be taken with caution. The further from the mean such estimates are made, the greater the error associated with them, and consequently the more caution that should be taken when interpreting them. Still, this elasticity provides a quantitative measure of the impact of railcar availability on the market for grain in much of this country.

Implications for the Grain Market

The relationship between adequate rail transportation and the prices farmers receive or consumers pay for grain is masked by myriad factors. This analysis demonstrates empirically that railcar availability influences grain price spreads between country and export markets. It further indicates that price spreads increase as the availability of railcars for grain service decreases. This finding and its implications are important to producers and buyers of U.S. grain.

Price spreads represent the marketing margins that separate farm prices for grain from those paid by buyers in destination markets. As this analysis suggests, decreases in the availability of railcars increase these spreads or margins. How the increases in marketing costs are passed on to the producer and buyer depend upon the relative elasticities of supply and demand. The more inelastic supply is relative to demand, the greater the share of the cost passed on to the farmer in the form of reduced prices for his or her production.[44]

Farmers bear a greater proportion of increases in marketing margins because grain supply at the farm level is generally more price inelastic then domestic or export demand.[45] Domestic wheat supply and demand have both been estimated to be price inelastic. The price elasticity of domestic supply has been estimated at .23, and the price elasticity of domestic demand has been estimated at –.25.[46] Based on these estimated elasticities, increases in price spreads impact farm-level prices more than domestic consumer prices. In the domestic grain market, increased price spreads resulting from inadequate railcar supply decrease grain prices at the farm level and increase grain prices for domestic consumers.

Estimates of short-run price elasticity for export wheat demand have been found to vary widely from a highly inelastic –.14 to a highly elastic –3.3. While most short-run estimates of price elasticity for export wheat demand have tended to be in the inelastic range, less conclusive studies of long-run price elasticities have tended to show long-run demand to be highly elastic.[47] Two separate studies have found that the price elasticity of export wheat demand, even in the short run, was very elastic and in the range of –2.5 to –3.13.[48,49] If the price elasticity of export wheat demand is highly elastic, given the inelasticity of domestic supply, increases in the spread between country and export prices that result from railcar supply problems are reflected almost entirely in the farm price. Observations made by other researchers support this conclusion. They suggest that farm prices, in many markets, are set by the country elevator by subtracting transfer costs from the offer price given by the exporter, who sets his or her price subject to world demand.[50]

As illustrated in figure 3, shifts in export demand increase both the quantity of U.S. grain demanded and the price of the grain in the export market. Railcar supply problems limit the market's ability to consistently supply grain to world buyers and to pass price increases on to U.S. farmers. As elasticity estimates indicate, U.S. farmers bear the greatest share of margin increases caused by railcar supply problems through lower farm prices and lower export volumes. U.S. grain exports are also affected. As price spreads increase, the price world buyers must pay for U.S. grain increases, making U.S. grain less competitive and alternative sources more attractive.

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[44] Dahl and Hammond, p. 157.

[45] Koo, p. 188.

[46] Oscar R. Burt, Won W Koo, and Norman J. Dudley, "Optimal Stochastic Control of U.S Wheat Stocks and Exports," *American Journal of Agricultural Economics*, vol. 62 (1980), pp. 173–174.

[47] Walter H. Gardiner and Praveen M. Dixit, *Price Elasticity of Export Demand. Concepts and Estimates* (Washington, DC: U.S. Department of Agriculture, Economic Research Service, February 1987), pp 14–15.

[48] Burt, Koo, and Dudley, p. 175.

[49] Panos A Konandreas and Andrew Schmitz, "Welfare Implications of Grain Price Stabilization: Some Empirical Evidence for the United States," *American Journal of Agricultural Economics*, vol. 60 (1978), p. 79.

[50] S. Fuller and C.V Shanmughan, "Effectiveness of Competition to Limit Rail Rate Increases Under Deregulation: The Case of Wheat Exports from the Southern Plains," *Southern Journal of Agricultural Economics*, vol. 13 (1978), p. 18.

Conclusions

Adequate railcar capacity is critical to the efficient marketing of U.S. grain. Adequate capacity allows grain farmers and shippers to quickly respond to changing marketing opportunities that can raise grain prices and profitability for their operations. A properly sized railcar fleet is also essential to the competitiveness of U.S. grain in a world market where alternative sources are readily available.

Railcar availability affects domestic and export grain prices in the United States. Reductions in the supply of available railcars increase grain price spreads between the farm and port. As the result of increased price spreads caused by railcar shortages, price levels can rise at port elevators without significantly increasing prices for grain at the country level. This is consistent with anecdotal information from grain exporters, traders, shippers, and farmers during past railcar shortages.

The model of grain price spreads estimated in this analysis suggests that corn and wheat price spreads may increase or decrease, on average, by as much as 1 cent per bushel in the study markets when the number of available railcars changes by as little as 1,477 cars per day. This level of variation in railcar availability is relatively small in comparison to the –5,287 to 16,244 car per day range actually observed during the 1986–89 period. With domestic supply more inelastic than domestic or export demand, the largest share of the change in price spread is borne by U.S. producers through the prices they receive for their grain. Price increases at the port, which can result from widening price spreads, also influence the competitiveness of U.S. grain in the world market. This analysis of grain price spreads suggests that reductions in railcar availability and railcar shortages result in lower farm prices and reduced competitiveness for U.S. grain exports.

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Appendix A: Assessing Correlation Among The Variables In The Model

The economic theory that provides the basis for understanding spatial price spreads also suggests that many of the factors that determine these spreads are not independent. The matrix of simple correlation provided in appendix table AA indicates, as might be expected, that some of the variables used in this model are correlated. This correlation is of particular concern for the variables used to measure local grain supply, exports, rail shipment volumes, and railcar availability. Table AA shows that the most serious correlation exists between exports (EX) and rail shipment volumes (RV). These two variables have a correlation coefficient of .54. Table AA also indicates that exports and railcar availability (RA) are correlated, but to a lesser extent, with a correlation coefficient of –.32. Rail volumes are further shown to be correlated with local supply (LS) with a correlation coefficient of .36. These values agree with what would be expected, given the real world factors that relate these variables.

The regression model was modified and its parameters re-estimated dropping separately the local supply variable, the export variable, and the rail shipment volume variable (LS, EX, and RV). The results of these regressions are provided in appendix table AB. Only by dropping the export variable from the original model do the estimated coefficients and their t–ratios change substantially. This, however, had almost no real effect on the explanatory capability of the model. Dropping the local supply or rail volume variables had no effect on the ability of the model to explain price spreads or the magnitude and significance of the estimated coefficients for the remaining variables. For these reasons and because the original model is more consistent with the theoretical factors that are thought to influence price spreads, the three variables were all included in the final regression equation.

Appendix Table AA—Correlation matrix for the variables used in the model

Correlations:	SPREAD	TBILLS	EX	LS	RV	RR	RA
SPREAD	1.0000						
TBILLS	.1661	1.0000					
EX	.2127	.0894	1.0000				
LS	.0887	–.1545	.0251	1.0000			
RV	.1759	.0545	.5383	.3547	1.0000		
RR	.5672	.1782	–.1634	.1308	–.1226	1.0000	
RA	–.2359	–.0848	–.3170	–.0143	–.1662	–.0733	1.0000

Appendix Table AB—Estimated parameters for regression model with selected variables dropped

	LS Dropped		EX Dropped		RV Dropped	
Variable	Beta	t-ratio	Beta	t-ratio	Beta	t-ratio
(Constant)	0.58156	10.146 *	0.71574	12.710 *	0.57820	10.136 *
EX	2.1729E-06	4.840 *			2.4322E-06	6.526 *
LS			7.5673E-08	1.114	6.4165E-08	0.962
TBILLS	0.02760	5.161 *	0.03169	5.267 *	0.03008	5.084 *
RV	1.4565E-06	1.091	5.0412E-06	4.468		
RR	0.08949	1.794 ***	0.09976	1.955 **	0.09227	1.843 ***
RA	–6.7841E-06	–4.573 *	–9.2983E-06	–6.579 *	–6.7740E-06	–4.565 *
QONE	–0.02525	–1.632 ***	–0.01401	–0.866	–0.02167	–1.359
QTWO	–0.04707	–3.137 *	–0.04343	–2.657 *	–0.04175	–2.602 *
QTHR	0.03968	2.565 *	0.02906	1.844 ***	0.04190	2.668 *
CRN	–0.12895	–3.731 *	–0.25638	–4.208 *	–0.15746	–2.675 *
CO	–0.16344	–3.895 *	–0.25478	–4.084 *	–0.19268	–3.184 *
ID	–0.32210	–7.324 *	–0.45637	–7.446 *	–0.34584	–5.728 *
KS	–0.19741	–3.979 *	–0.35051	–4.497 *	–0.22535	–3.063 *
MN	–0.02181	–0.813	–0.06233	–1.383	–0.05581	–1.261
MT	0.10822	2.306 **	–0.04845	–0.734	0.08569	1.330
NE	–0.13265	–4.470 *	–0.22191	–3.963 *	–0.16391	–3.026 *
ND	0.08417	1.674 **	–0.09308	–1.182	0.04598	0.588
OK	–0.19739	–4.314 *	–0.30900	–4.699 *	–0.22242	–3.521 *
OR	–0.51660	–10.835 *	–0.64340	–10.213 *	–0.54003	–8.693 *
TX	–0.15416	–3.109 *	–0.28193	–4.031 *	–0.17642	–2.657 *
WA	–0.49928	–10.551 *	–0.64128	–9.658 *	–0.52504	–8.054 *
Adj. R-squared	0.72097		0.71017		0.72084	
Std Error	0.12859		0.13105		0.12862	
N =	593		593		593	
F =	77.48306 *		73.53047 *		77.43386 *	

Note * Indicates significantly different from zero at the .01 confidence level.
** Indicates significantly different from zero at the .05 confidence level.
*** Indicates significantly different from zero at the .10 confidence level.

Testimony of

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Business and Public Policy, College of Business
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to
Joint Committee Meeting of
U.S. Senate & House of Representatives
Committees on Small Business

November 8, 1995

1100 Longworth House Office Building
U.S. House of Representatives

Washington, DC

INTRODUCTION

My name is Curtis M. Grimm, and I am Professor and Chair of Transportation, Business and Public Policy, College of Business and Management, University of Maryland at College Park. I have been a member of this College since 1983. I received my B.A. in economics from the University of Wisconsin-Madison in 1975 and my Ph.D. in economics from the University of California-Berkeley in 1983. My Ph.D. dissertation investigated competitive impacts of railroad mergers.

My background includes extensive involvement in development of public policy regarding transportation, including ICC merger adjudication. I have previously been employed by the Wisconsin Department of Transportation, the U.S. Interstate Commerce Commission, and the Australian Bureau of Transport and Communication Economics and have consulted for several other government agencies and private firms regarding transportation issues. I served as Assistant to the Chief of Intercity Transport Development, Planning Division, Wisconsin Department of Transportation in two separate stints between 1975 and 1978, with a focus on rail policy issues such as abandonments and the creation of shortline railroads. I also worked on a consolidation involved competing bids from Burlington Northern and the Soo Line/Milwaukee Road/CNW for the Green Bay and Western Railroad, decided by the ICC in 1977.

While serving as an economist at the ICC's Office of Policy Analysis from January to December 1981, my duties included analysis

of competitive effects for the Union Pacific-Missouri Pacific-Western Pacific merger. During 1982, I served as a consultant for the Commission while the UP-MP-WP decision was being drafted and subsequently for the ICC in the Ex Parte No. 347 decision ("Coal Rate Guidelines - Nationwide").

Recently, I have participated in several ICC rail merger proceedings, including a proposal by Wisconsin Central ("WC") to control the Green Bay & Western ("GBW") and Fox River Valley ("FRVR") railroads and the proposed Union Pacific-Southern Pacific merger. Specifically, I have provided testimony evaluating the competitive consequences of these transactions.

My research has involved deregulation, competition policy, competitive interaction and management strategy, with a strong focus on transportation. This research has resulted in over 60 publications, including articles in leading journals such as Journal of Law and Economics, Transportation Research, Transportation Journal, Logistics and Transportation Review, Academy of Management Journal, Management Science, Strategic Management Journal, and Journal of Management. More than two dozen publications have dealt specifically with the railroad industry, mainly on deregulation, mergers, and competition issues. I have also co-authored three monographs.

In summary, I have had extensive experience conducting and evaluating research regarding railroad mergers and direct exposure to ICC merger analysis. My position regarding the impacts of rail mergers that are anticompetitive, based on this research and experience, remains as stated in my 1990 Brookings co-authored

monograph:

> As Alfred Kahn and others have noted of the airline industry, it is important to recognize that deregulation did not authorize the government to abdicate its antitrust responsibility and to fail to take actions to preserve competition. To the extent that mergers can enable railroads to improve service and reduce costs without concomitant anticompetitive effects, they should be encouraged. It is the ICC's responsibility to scrutinize carefully potential anticompetitive effects from both parallel and end-to-end mergers. In particular, a policy of continuing to discourage parallel mergers appears to be in order. (Winston, Corsi, Grimm, and Evans; 1990, p. 54).

The remainder of this statement elaborates on this position, that deregulation has resulted in significant benefits, but that rail competition must be maintained in order to preserve these benefits.

II. U.S. RAIL DEREGULATION AND RAIL INDUSTRY REVIVAL

A dramatic and fundamental change has occurred in U.S. railroad policy in recent years. This section will detail the changes in policy which have taken place in railroad regulation and the industry response to deregulation.[1] Prior to 1980, U.S. railroads were overwhelmingly burdened by an outmoded regulatory framework, and found themselves hampered by regulations that were causing them to lose more and more traffic, contributing to a serious deterioration of the country's entire railroad industry.

As a result of pressures to save the industry from total bankruptcy, and coinciding with a general trend towards

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[1] This section draws from Grimm and Rogers (1991).

deregulation of U.S. industry, the Railroad Revitalization and Regulatory Reform Act (the "4-R Act") and, in particular, the Staggers Rail Act of 1980 granted substantial new freedoms to the railroads, including virtually complete pricing flexibility. More specifically, railroads were provided additional freedom to set rates via new provisions on commodity exemptions, confidential contracts and maximum rate determination. ICC rate regulation now remains on only a small fraction of traffic. In addition to traffic exempt from regulation or moving via contract, the 4-R Act and Staggers Act have also provided substantial additional rate flexibility on other traffic.[2]

As discussed in more detail by Roberts (1987), the ICC adopted maximum coal rate guidelines in 1985 which introduced an approach of "constrained market pricing." These guidelines are predominantly market based, with the only long-term constraint on railroad rates being that they are not to exceed "stand-alone costs" of service.[3] Decisions in several rate cases indicate that the net effect of the post-Staggers maximum rate regulation has been to place limited restraint on the ability of railroads to raise rates. Indeed, rates have been rolled back by the ICC in only a handful of cases.

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[2] To successfully challenge a rate as unlawful, a shipper must essentially overcome three hurdles. First, the rate must exceed 180% of variable costs. Second, the ICC must determine that the railroad has no effective competition for the movement in question, i.e., that it is market dominant. Third, the ICC must determine that the rate is unreasonable.

[3] The stand-alone cost approach allows shippers to estimate the lowest rate at which a hypothetical, efficient competitor would be adequately compensated. The shipper is allowed to incorporate both costs and revenues of other traffic on the simulated system.

The U.S. railroad industry has experienced a dramatic improvement in its financial condition since the Staggers Act.[4] My co-authors and I (Winston, Corsi, Grimm, and Evans; 1990) have conducted the most comprehensive study of the effects of both rail and truck deregulation, employing a counterfactual methodology. In other words, rail profits, rates, revenues, costs and service levels in 1977 were compared with estimations of what values would have prevailed in 1977 had the industry been deregulated. Unlike historical comparisons of values over time, this methodology allows for control of non-deregulation impacts on railroads, such as inflation, the state of the economy, etc.

According to this study, the railroads reaped annual profit gains of $2.9 billion dollars per year (1988 dollars) from deregulation, with cost savings of over $3 billion dollars due to deregulation (pp. 15-41). This confirms that deregulation has resulted in substantial financial benefits to the railroads, with cost savings being the most prominent. Customers have also reaped substantial benefits from both rail and truck deregulation.

In sum, U.S. deregulation was intended to provide a greater reliance on free markets to promote railroad profitability and public benefits. Financial data and counterfactual studies support the notion that the Staggers Act has greatly contributed to a

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[4] As discussed above, the poor financial condition of the industry, punctuated by a number of rail bankruptcies provided the primary motivation for railroad deregulation. Indeed, by 1979, almost one-fourth of Class I rail mileage was in bankruptcy and from 1971-1980, railroad return on equity averaged less than 3% (MacDonald, 1993). Since Staggers, not one major railroad has gone bankrupt and the financial condition of the industry has improved dramatically.

revitalization of the U.S. rail freight industry.

III. THE BENEFITS OF DEREGULATION DEPEND ON PRESERVING AND PROMOTING RAIL COMPETITION

One of the essential premises underlying the deregulation of transportation, communications and other industries is that in the absence of price and entry regulation, these industries would be sufficiently competitive to generate improvements in allocative, technical and dynamic efficiency in each industry. However, competition must be preserved and promoted for this premise to be realized. As I stated in the conclusion of my 1984 article entitled "Promoting Competition in the Railroad Industry: A Public Policy Analysis":

> The preceding analysis has demonstrated the importance of preserving and promoting competition. At stake are billions of dollars in economic benefits as well as perhaps the very success of rail regulatory reform.
>
> The implications are clear: rail intramodal competition must be encouraged in every relevant area...Competition should be preserved and promoted now, as undoing misguided actions will not be easy (Grimm, 1984, p. 227).

This competition between rail carriers is absolutely critical to protecting shippers, especially small shippers, from price increases. The importance of rail competition in influencing rate levels has been supported by a number of econometric studies.[5]

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[5] A study by the author (Grimm; 1985) gathered 1977 data on rail rates and degree of rail competition in 110 rail markets, as defined by specific origin-destination pairs. The study found a significant relationship between rates and rail competition at origin and destination, with added competition causing lower rates. Additionally, the Brookings Institution study to which I have previously referred (Winston, Corsi, Grimm, Evans, 1990) supported the importance of railroad competition in reducing rail rates. Using 1985 data drawn over a large number of origin-destination

Particularly relevant to this Committee are two studies by MacDonald (1987, 1989), which have used post-Staggers data to investigate the impact of rail competition on rates for agricultural commodities. One study uses 1983 data for shipments of corn, soybeans and wheat, with regressions being performed to ascertain the relationship between rates and rail competition. MacDonald concludes: "The analysis shows an important, statistically significant effect of concentration on prices in an industry with high barriers to entry and large capital commitments." A second study draws on data from 1981-1985 regarding grain shipments. It concludes: "Competition among railroads has a statistically significant, fairly strong effect on rates. More competitors, --- are associated with lower rates. The addition or subtraction of a competitor has a larger effect on rates, the fewer the number of competitors in a market.

In an actual merger case, it is often times hard to gauge the impact of mergers on such shippers because there is a disincentive for shippers to come forth in merger cases, even if they believed that anticompetitive effects might result. In this era of close partnerships between shippers and carriers, a shipper risks alienating a railroad by publicly opposing a rail merger. A shipper in such an instance must weigh the negative effects of speaking out (loss of leverage, disruption of working relationships, and possible retaliation) against the positive possibility that a given statement may make the difference in

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pairs, the authors found that price-marginal cost margins were significantly lower in markets with a greater degree of railroad competition.

determining policy. Shippers may face significant harms from the transaction, but still judge from a self-interested perspective that the risks of speaking out are greater than the benefits.

IV. PARALLEL RAIL MERGERS: CURRENT ISSUES

In order to determine whether adequate rail competition is being maintained it is important to analyze the current merger standards and whether they are adequate for future mergers. This is especially important as the number of large rail carriers declines due to further consolidations. The Interstate Commerce Commission has authority regarding railroad mergers in the U.S. Modern authority dates back to the Transportation Act of 1940, which amended section 5(2) of the Interstate Commerce Act and required the ICC to approve consolidations which furthered the public interest. As part of the merger deliberation process, the Antitrust Division of the Department of Justice has played an active role in assessing competitive harms. The DOJ has found that a number of proposed rail mergers raise important competitive concerns and has opposed or requested competition-preserving conditions in a number of cases.[6]

The 4-R and Staggers Acts, along with ICC administrative actions, encouraged end-to-end consolidations and set off a railroad merger wave. As a result, the U.S. railroad system has gone through a major restructuring in the early 1980s, leaving 3

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[6] Recently, for example, in a proposed merger of three relatively small railroads in Wisconsin (Wisconsin Central, Fox River Valley and Green Bay and Western), the DOJ participated actively and found serious competitive problems with the merger. Despite DOJ's concerns the ICC approved the merger without any conditions, other than a monitoring condition.

large systems dominant in the East and 4 major roads dominant in the West. It is critical to note that the major consolidations since Staggers have been primarily end-to-end. The ICC denied the largely parallel Southern Pacific-Santa Fe proposed consolidation in the mid 1980s. Recently, the consolidation of the Burlington Northern and Santa Fe reduced the number of dominant Western railroads to three.

The ICC now is at a critical juncture with regard to preserving rail competition. The proposed Union Pacific-Southern Pacific merger has unprecedented parallel effects and will result in elimination of rail competition in many Western markets. In conjunction with the BN-Santa Fe merger, where competition remains in the West, the BN-Santa Fe and UP-SP will dominate the entire West. Additionally, the ICC may well be faced with a parallel merger proposal involving the 3 dominant Eastern carriers and then eventually East and West railroads, potentially leaving only two major railroads in the entire U.S.

V. POLICY OPTIONS

I have long argued for policies which would preserve and promote rail competition (Grimm; 1984). Of particular relevance today is rail merger policy. In light of past, present and potential future rail consolidations and past evidence showing that as railroads consolidate rates charged to shippers go up, it is imperative that a serious analysis of the current ICC merger standards be conducted. In my opinion, the importance of competition in ICC rail merger decisions should be given more

deference, with more weight being given to evidence of a reduction in competition and with substantial deference being given to the DOJ's views in this regard. Under current standards, the ICC could approve a significantly anticompetitive merger, based on claims of speculative efficiency gains which would outweigh competitive harms. Importantly, if the Commission fails to act and rail competition is further reduced, much more aggressive action will be needed in the long run to provide the needed competition for rail shippers. The Canadian model provides one such example of what this might entail.[7]

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[7] The 1987 National Transportation Act included several provisions to increase rail intramodal competition, in particular for shippers captive to a single railroad. Most importantly, the Canadian interswitching legislation promotes such competitive access in a more vigorous manner than U.S. reciprocal switching legislation. Such access is provided to shippers primarily within an urban area through rates set by government fiat. Dating back to 1908, interswitching was required within distances of 4 miles. In other words, assume a coal mine has physical access to only one railroad (Railroad A), but is located within four miles of a second railroad (Railroad B). The coal mine can arrange to ship its coal with Railroad B, with Railroad A required to move the coal from the mine to the junction with Railroad B at prescribed rates. The 1987 legislation extended this to 30 kilometers and also provided the National Transportation Agency to set compensatory rates for such interswitching, to be adjusted annually. Shippers outside this limit who compete with shippers within the 30K limit can apply to be deemed within the limit. According to the National Transport Agency of Canada (1992), Canadian National and Canadian Pacific currently interswitch between 130,000 and 140,000 cars annually, with half that volume outside the previous 4 mile limit. According to the National Transportation Act Review Commission (1992), the percentage of shippers having access to two or more railroads has increased from 54% to 80% because of the extension of the interswitching limit.

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STATEMENT OF C. PHILLIP HOFFMAN, SECRETARY
HOFFMAN & REED, INC., TRENTON, MISSOURI

House and Senate Committees on Small Business
Representative Jan Meyers, Chair
Senator Christopher Bond, Chairman
November 8, 1995

I am Phil Hoffman representing Hoffman & Reed, Inc., a firm which my brother and myself manage. Hoffman & Reed, Inc. is a family owned country elevator and farm supply firm handling grain, feed, seed, fertilizer and crop protection inputs; with 33 employees located in Trenton, Missouri. Trenton is a town of 6,500, located in north Missouri on what was originally the Rock Island Railroad's spineline running from Minneapolis to Kansas City. Our business was started in 1949 by my uncle and my father (both still active) selling sacked feed and buying cream and eggs from local farmers. In 1952 we started direct loading rail cars; 55 boxcars were loaded that first year. The elevator began expanding and today we have total storage capacity 1,900,00 bushels in two locations with ability to load 12 to 15 hoppers per day.

In the 1960's the Union Pacific petitioned the ICC to purchase the Rock Island. After some 12 years of deliberation the proposed sale was denied by the ICC. In March 1980 the Rock Island filed bankruptcy. Following a couple of years of directed service by the KCT, the Chicago Northwestern (CNW) purchased the remaining tracks of the Rock Island. The CNW invested in the line and brought train speed up to 50 mph from 5-10 mph the Rock Island was operating on following years of neglect. For 12 years we have enjoyed a good relationship and much improved service with the CNW.

This past spring the Union Pacific Railroad (UP) acquired the CNW and the two systems merged operationally October 1, 1995. Since the fall of 1994 car supply has been tight, however the problem has accentuated since the UP took over operationally. Over the past 6 years we have loaded 350-400 hoppers per year consisting of four commodities; soybeans, wheat, corn and milo. We also have averaged receiving 35-40 cars of fertilizer over the last 8 years. In 1995 we have loaded 208 cars and only 5 since fall harvest (our peak shipping season) began, which also coincided with the UP taking over operationally. We fully expected difficulties this fall with rail service. We knew cars were tight and we suspected the transition from the CNW to the UP would not be smooth. The one silver lining of the small crop harvested in our area this fall was that we were able to handle the crop with few problems even with basically no rail cars. Our biggest concern is the future.

From conversations with the CNW, UP and processors and elevators receiving our grain, we have been given little encouragement for improvement any time in the near term, if at all. All indications point to the UP being committed to a program of shuttling large unit trains of 75-100 cars between large shippers and large users. The potential benefits of the UP we saw for Hoffman & Reed, Inc. and our farmer customers in terms expanded access to additional markets through the UP system will mean little if we don't receive hopper cars to load.

We understand and fully expected change with this merger. We also understand growth and the efficiencies the mega railroads are attempting to accomplish. However, if the mega railroads are unable or unwilling to provide service to small shippers, then opportunities should be devised for others who are willing to provide that service.

Thank you for the opportunity to tell our story.

MY NAME IS JAMES F. JUNDZILO,

I AM THE TRANSPORTATION MANAGER FOR TETRA CHEMICALS. I HAVE 30 YEARS EXPERIENCE IN THE TRANSPORTATION AND DISTRIBUTION PROFESSION. INCLUDING ACADEMIC, CONSULTANT AND OPERATION MANAGEMENT. I HAVE A MBA, ICC PRACTITIONER AND CERTIFIED MEMBER OF AMERICAN SOCIETY OF TRANSPORTATION AND LOGISTICS. I AM RESPONSIBLE FOR RAIL NEGOTIATION AND RAIL SERVICE STRATEGY FOR TETRA CHEMICALS. TETRA CHEMICALS IS A CONSUMER OF RAIL SERVICE. THE SERVICE REQUIREMENT IS NORTH AMERICA. TETRA CHEMICALS UTILIZES ALL MAJOR CLASS ONE RAILROADS. VOLUME IMPACT TO THE CLASS ONE RAILROADS IS MARGINAL, TETRA CHEMICALS HAS LESS THAN 800 RAILCAR MOVEMENTS THUS RAILROAD CONSOLIDATION AND MERGERS IN MOST CASES HAVE A NEGATIVE IMPACT ON TETRA CHEMICALS.

THERE ARE BASICALLY THREE ASPECTS I WOULD LIKE TO COMMENT ON IN REGARDS TO THE ABILITY OF

SMALL BUSINESS TO USE RAIL. THEY ARE:

- ABANDONMENT
- REVENUE REQUIREMENTS
- ROUTE RESTRICTIONS

THE CLASS ONE RAILROADS HAVE ABANDONED TEAM TRACKS SPACE, SIDE TRACKS AND SOLD BRANCH LINES. I BELIEVE THIS WAS A DIRECT RESULT OF CONSOLIDATION OF TWO MAJOR EASTERN RAILROADS FOR EXAMPLE IN 1995 TETRA CHEMICALS USED TEAM TRACKS, SIDE TRACKS AND BRANCH LINES IN THE STATE OF VIRGINIA TO DELIVER PRODUCT TO THE CUSTOMER..

THERE WERE MANY TIMES I COULD NOT USE THE MOST EFFICIENT LOCATION BECAUSE OF THE NEWLY ABANDONED TRACK, RESULTING IN HIGHER COST AND POOR DELIVERY SERVICE. AS A SMALL BUSINESS WHAT OPTIONS DO I HAVE? VOLUME SPEAKS, NOT A FEW RAILCARS TO A SIDE TRACK. THE CLASS ONE RAILROADS APPEAR TO BE STRIPPING DOWN THE TRACK CAPACITY TO ELIMINATE JUST THE TYPE OF

TRACK WE NEED TO DO BUSINESS. ANOTHER ASPECT IS THE BRANCH LINES AVAILABLE TO TETRA, IN MOST CASES ARE CAPTIVE ON THE CLASS ONE RAILROAD WHO SPIN THEM OFF.

THE RAILROAD WHO CONTROLS THE DESTINATION CAN DICTATE THE WHOLE SERVICE ROUTE WHETHER IT MAKES SENSE OR NOT.

FACT IS, EAST OF THE MISSISSIPPI RIVER HAS BEEN REDUCED TO THREE PRIMARY RAILROADS.

THE JUSTIFICATION HAS BEEN THAT VOLUME IS NOT THERE. THE REALITY IS COMPETITION KEEPS TRAINS RUNNING, A MERGER REDUCES THE NEED FOR COMPETITION. THUS SMALL BUSINESS HAS TO GIVE UP THE MORE ECONOMICAL RAIL OPTION BECAUSE THE CLASS ONE RAILROADS HAVE DECIDED THE VOLUME AND REVENUE IS NOT JUSTIFIED.

SMALL BUSINESS RAIL VOLUME IS TRANSFERRED TO TRUCK BECAUSE IT FALLS UNDER A REVENUE REQUIREMENT OR NOT ENOUGH CAR MOVEMENTS. THIS RAIL VOLUME WOULD BE BEST SERVED ON RAIL. THE CONSUMER IS

FORCED TO USE TRUCKS. REVENUE REQUIREMENTS NORMALLY MEANS A RECOVERY LEVEL TO OPERATE. THERE IS ANOTHER MEANING WHICH IS IF WE HAVE A REVENUE BASIS FROM POINT A TO POINT B AND TETRA IS SHIPPING FROM A NEW LOCATION POINT C TO POINT B THEN THE RAILROAD WILL TRY TO MAINTAIN THE SAME REVENUE BASIS REGARDLESS OF RAIL OPERATING EFFICIENCIES. THIS CAN BE A MAJOR ISSUE FOR SMALL BUSINESS RAIL SHIPPERS. IF RAIL IS OUR ONLY CHOICE HOW DO WE DEAL WITH A PURELY MONOPOLISTIC "TAKE OR LEAVE IT". THIS USUALLY ENDS UP LOST RAIL BUSINESS BECAUSE THE SMALL BUSINESS WITHDRAWS FROM TRYING TO MARKET IN THESE AFFECTIVE MARKET AREAS.

ANOTHER RESULT OF RAIL MERGERS IS THE IMPACT ON COMPETITIVE ACCESS, OUR LAKE CHARLES LA. PLANT HAS THREE RAILROADS: UNION PACIFIC (MP), SOUTHERN PACIFIC AND KANSAS CITY SOUTHERN. POINT OF FACT UNION PACIFIC USES A SWITCHING CARRIER TO SERVICE

OUR PLANT. THE ISSUE WITH COMPETITIVE ACCESS IS LIMITED BY THE DESTINATION CARRIER. THUS If SOUTHERN PACIFIC OR THE UNION PACIFIC DELIVERS KANSAS CITY SOUTHERN WOULD BE DISCOURAGED FROM PARTICIPATION IN JOINT ROUTES. ON PAPER IT APPEARS WE HAVE COMPETITIVE ACCESS , IN FACT, WE ARE RESTRICTED TO THE THROUGH CARRIER. ANY WESTERN STATE RAIL BUSINESS HAS TO BE ROUTED ON THE UNION PACIFIC OR SOUTHERN PACIFIC. WE CANNOT ROUTE THE KANSAS CITY SOUTHERN. THUS KANSAS CITY SOUTHERN RAILROAD IS RELEGATED TO A REGIONAL BASED CARRIER.

NOW CONSIDER CAPTIVE SHIPPERS POSITION, WHICH MEANS ONE RAILROAD SERVICE. TETRA HAS TWO PLANTS THAT WOULD BE CONSIDERED CAPTIVE. BOTH PLANTS HAVE WATER/BARGE ACCESS. IF I SHIP ONLY ON THE WATERWAY SYSTEM COMPETITIVE CONDITIONS NORMALLY EXIST. HEAVEN HELP ME IF I HAVE TO GO INLAND. CAPTIVE HURTS MOST IF ONLY ONE RAILROAD CONTROLS DESTINATION. BECAUSE OF ROUTE

RESTRICTIONS COMPETITIVE ACCESS CAN BE JUST AS MUCH CAPTIVE AS A SINGLE RAIL SERVICE.

IF UNION PACIFIC AND SOUTHERN PACIFIC MERGE I WOULD ONLY HAVE ONE RAILROAD TO GO WEST BECAUSE OF THE ROUTE LIMITATION. THIS WOULD AFFECT TETRA CHEMICALS WICHITA KANSAS PLANT THE RAIL SERVICE HAS BEEN REDUCE BY ONE BECAUSE OF THE BURLINGTON NORTHERN AND SANTE FE MERGER. I FEEL THIS WILL HAVE A NEGATIVE IMPACT ON TETRA CHEMICALS BECAUSE OF THE LACK OF COMPETITION IN THE SERVICE AREA. THE CAPTIVE DESTINATION SERVICED BY THE ORIGINATING CLASS ONE RAILROADS.

RECOMMENDATION 1: OPEN ROUTING WHICH MEANS I SHOULD BE ABLE TO ROUTE MY RAIL CARS OVER CITIES IF MORE THAN ONE RAILROAD EXIST IN THE COMMERCIAL ZONE. WHY SHOULD I BE LIMITED TO ONLY TWO OR THREE GATEWAYS.

RECOMMENDATION 2: ORIGINATING AND DELIVERING CARRIERS SHOULD BE REQUIRED TO MAKE ROUTES AT THE

SAME PRICE AS THROUGH ROUTES OR SINGLE LINE. I SAY THIS BECAUSE WHEN A SINGLE LINE MOVES WEST THE SINGLE LINE GOES THROUGH THE SAME INTERCHANGE OPERATING ENVIRONMENT AS JOINT LINES. FOR EXAMPLE MP WHICH IS UNION PACIFIC IN THE GULF COAST INTERCHANGES WITH THE UNION PACIFIC AT KANSAS CITY. THE ACTION MIGHT OCCUR AGAIN AT PROVO UT GOING WEST TO STATE OF WASHINGTON OR STATE OF CALIFORNIA.

RECOMMENDATION 3: REVENUE REQUIREMENT NEEDS DEFINITION AND APPLICATION RULES. THE CLASS I RAILROAD SHOULD BE REQUIRED TO MAINTAIN TEAM TRACKS AND SIDE TRACKS FOR PUBLIC NEED AND NECESSITY.

IN SUMMARY IF I ONLY HAVE TWO RAILROADS SERVING THE WESTERN UNITED STATES THE ABOVE RECOMMENDATIONS ONE AND TWO WOULD BE OBSOLETE. THE POTENTIAL MERGER OF THE UNION PACIFIC AND SOUTHERN PACIFIC WILL HAVE DIRE CONSEQUENCES FOR

THE SMALL BUSINESS. A LOT OF WORK TO UNDERSTAND THIS MERGER NEEDS TO BE DONE BEFORE WE LOCK THE WESTERN STATES WITH ONLY TWO RAILROADS. I WOULD HIGHLY RECOMMEND TO LOOK TO THE EASTERN STATES AS INDICATIVE OF TOO FEW RAILROADS.

THANK YOU FOR THE OPPORTUNITY TO PRESENT MY VIEWS.

Testimony of

Fredrick D. Palmer
General Manager & Chief Executive Officer
Western Fuels Association, Inc.

to
Joint Committee Meeting of
U.S. Senate & House of Representatives
Committees on Small Business

November 8, 1995

1100 Longworth House Office Building
U.S. House of Representatives

Washington, DC

Western Fuels Association, Inc. is delighted by the attention of the House and Senate Small Business Committees to the impact on the nation's businesses of recently approved, proposed, and still-rumored mergers among the few remaining Class I railroads in the United States. Our concern centers on the increased potential for monopolist abuse of captive shippers.

I am especially delighted to appear on this morning's panel with the Secretary of Agriculture. Secretary Glickman was one of the captive shippers' earliest allies when he represented Kansas in Congress. As an original cosponsor of both the Railroad Antimonopoly Act and the Clayton Act Amendments in the 99th and 100th Congresses, Mr. Glickman led a bi-partisan coalition of diverse groups in tackling this problem — a problem, I might add, rendered all the more acute by recent changes both within the structure of the railroad industry itself and also within the structure intended to regulate and govern it.

It seems ironic that this problem receive its first airing during a joint meeting of your respected Committees because both captive shippers and the impact of the absence of real competition among railroads on businesses both small and large are not small at all. The impact is felt, every day, in key sectors of the nation's economy. What is at issue is the efficiency of free markets, fairness in interstate commerce, and fundamental principles of anti-trust law.

Let me be clear about one thing. Western Fuels Association is not here to bash railroads. As a producer, purchaser, and shipper of 23 million tons of coal to twelve consumer-owned electric utility power plants throughout the Great Plains, Rocky Mountain, and Southwest states, and in Louisiana — and as the largest single purchaser of coal from the Powder River Basin in Wyoming and Montana — Western Fuels Association, its member utilities, the entire coal industry and, indeed, the entire electric utility industry are partners with the nation's railroads in an enterprise central to our economy's continued vitality: electricity supply.

The industrial, commercial, and residential sectors of the national economy — fully ninety percent of our economy — consume 99.9% of all electricity. Each year, 300% more electricity is purchased than the second largest commodity, gasoline. The largest non-energy commodity is cattle, and electricity purchases are 600% greater. The industrial, commercial, and residential sectors of the economy today consume more of their primary energy in the form of electricity than as direct combustible fuels. Nearly 60% of that electricity is generated through the combustion of coal. That coal, over 700 million tons per year, moves by rail. In the overwhelming majority of instances there is no viable transportation alternative. The alternative, when there is one, is barge transportation at 150 million tons per year, and a large percentage of that is moved to or carried from port by rail.

Coal is the single largest commodity hauled by the industry and accounts for 40% of total freight tonnage carried by Class I railroads contributing 22% of total industry revenues.

As a direct consequence of the market freedoms embodied in the Staggers Rail Act of 1980, the nation's railroads have enjoyed tremendous benefits from

increased efficiency and consolidation. Today, railroads employ half as many people as they did then. They operate along a third fewer route miles using 34% fewer locomotives and 30% fewer railcars. Even so, they deliver 31% more ton-miles to their customers than they did in 1980, while earning 1.5 times more money, even while paying their remaining workers twice as much. From a railroader's perspective, Staggers works.

It should be clear then, the coal and electric utility industries depend upon the railroads and the railroads depend on us. But there is a sticking point in the relationship. Those shippers who have the means of securing competitive bids among railroads are paying less and less. Those of us who are captive shippers are paying more and more.

For shippers who are captive to a particular railroad, either at the point of origin (the coal mine) or destination (power plant), there is no enjoyment of the benefits of free markets and competition. This point could be no better illustrated than it is by an exchange of correspondence between Western Fuels and the Burlington Northern Santa Fe.

An affiliate of Western Fuels Association, Inc. (Western Fuels Service Corporation) applied to the Interstate Commerce Commission for trackage rights as a condition of the Commission's approval of the merger between the Burlington Northern (BN) and Atchison Topeka & Santa Fe (ATSF) railroads. We were not alone in making such a request, but we were singular in our proven record of successful operation of two railways: the Escalante-Western in New Mexico and the Deseret-Western along the Colorado and Utah border.

What we sought from the Commission was permission to operate our own rail equipment between the BN's junction with the Union Pacific (UP) system at a rail yard in Denver, then along the BN system to Pueblo and its junction with the ATSF, and from there to Sunflower Electric Power Corporation's Holcomb Power Station in western Kansas. We also proposed, in the alternative, Western Fuels operating along the ATSF from Pueblo, if BN hauled the coal to Pueblo.

Our motivation was the potential to create competition between the UP and BN at the coal's origin. At present, Sunflower pays millions of dollars per year in above-market costs, absent competition. Our concern — legitimate, we believe — is BN's potential to monopolize the entire coal haul once merged with ATSF, effectively constraining competition with the UP for the traffic. The continued economic viability of Sunflower's investment in its power plant is at stake in an increasingly deregulated utility environment, absent relief from its presently far-above-market rail rate.

Four years ago, Western Fuels sought trackage rights in behalf of our coal delivery obligation to another member, the Southern Minnesota Municipal Power Agency (SMMPA). Western Fuels supplies SMMPA's share of coal at the Northern States Power Company (NSP) Sherburne County (Sherco) power plant, north of the Twin Cities. NSP leverages competitive access to its Twin Cities power plants into a lower rate from the BN for shipments to Sherco than SMMPA is able to secure. Both NSP's and SMMPA's coal is of the same origin. The difference is, SMMPA is captive at Sherco and lacks NSP's competitive leverage. So Western Fuels sought trackage rights along the line from the Twin Cities. BN declined to negotiate.

How important are transportation rates to utilities? The cost of coal — most of which is the cost of hauling it — represents anywhere from one-third to more than one-half the price a utility charges consumers for electricity.

The ICC denied our trackage rights request (and that of virtually all other applicants) in approving the BN/ATSF merger. We have appealed that decision. But, nonetheless, on September 25, 1995 I wrote two letters to John Q. Anderson, senior vice president of BN's coal business unit. In one, I reiterated our request for negotiation of trackage rights to Holcomb. I pointed toward BN's voluntary grant of trackage rights to Southern Pacific and stated my belief that by this action, BN is obliged to voluntarily deal with Western Fuels Service Corporation under similar terms and conditions.

It is our view that under applicable Federal law, BN cannot discriminate among railroad competitors for the purpose of maintaining a monopoly position. As a "railroad" in our own right, we have potential for being a competitor.

My second letter concerned a request that Western Fuels Service Corporation be permitted trackage rights along the joint line in the Powder River Basin (PRB) where both the UP and BN already operate. Competition in the PRB is constrained, however, by a territorial restriction agreement between the two railroads for mines north of Gillette or, stated another way, competition between the two exists only south of Donkey Creek Junction.

Western Fuels' request for trackage rights concerned the route along that portion of the BN line north of Donkey Creek so that we could reach our own Dry Fork Mine and the Buckskin Mine operated by Triton Energy, our supplier for coal at

Cajun Electric Power Cooperative's Big Cajun No. 2 in New Roads, Louisiana and one of our suppliers to the Missouri Basin Power Project's Laramie River Station (LRS) at Wheatland, Wyoming. Success in that venture would create potential for competition between the BN and UP for coal deliveries to Big Cajun No. 2 and a number of other power plants that burn PRB coal.

My letter was clear. We would negotiate with the BN to establish a fair value for such trackage rights, taking into account BN's substantial investment in that track and various improvements it has made in the route. Nonetheless, BNSF's response was abrupt and back-of-the-hand.

The full text of all three letters is hereby submitted for this hearing record, but let me quote the relevant paragraph (of only two) in Mr. Anderson's response dated October 16. It is, in effect, Exhibit A in the case of captive shippers in their dealings with increasingly monopolistic railroads:

> ...we are not interested in granting trackage rights to any carrier over the routes you described in your letters. Your view that voluntarily granting trackage rights over other rail lines to other common carriers obligates us to grant trackage rights to any specific party over any specific part of our railroad is a novel idea, *but certainly not supported by any regulatory requirement of which we are aware*. We continue to provide excellent service at competitive rates to utilities throughout the country. The continued burning of BNSF-delivered PRB coal and the continued growth of this fuel at our existing customers' plants demonstrates that we are doing very well for them in a competitive market. [*Emphasis* added]

In other words, it is BNSF's view that the existence of competitive rates for *some* shippers proves the existence of competition. And BNSF's marketing savvy in holding onto their present customers in charging whatever the market will bear insofar as those utilities' ability to compete for sales of electricity, is given as further evidence that the free-market is working.

I submit that a virtually deregulated railroad system in serving a virtually deregulated electric utility industry cries out for the sorts of antitrust regulation to which both the electric utility and telecommunication industries are subjected. For too long, railroads have been able to hide behind a feeble vestige of regulation in the Interstate Commerce Commission (the Keogh doctrine) as protection from fundamental antitrust law. With it now abundantly clear that the railroads are more than happy to capitalize upon the deregulatory and free-market mood of the 104th Congress and do away with the ICC, it is time for this Congress to amend the antitrust laws in a way which permits unfettered competition for rail service and to see how free markets function in rail transportation.

There are alternatives as to how this can be accomplished. I would urge that Congress seriously consider those portions of Canadian transportation law which bear upon this question and have met with considerable success in effecting competition among carriers. You might consider amending the Clayton Act. Other remedies no doubt can be devised. In any case, in the face of increased merger and acquisition activity among railroads, it is important that Congress pay close attention to the potential for anti-competitive practices by the remaining carriers and to the need for competitive access to essential facilities in order to assure effective functioning of free markets. I commend your Committees for your early and timely attention to this need.

APPENDICES

WESTERN
FUELS
ASSOCIATION
INC.
The National Fuel Supply Cooperative

Fredrick D. Palmer
General Manager and Chief Executive Officer

September 25, 1995

John Q. Anderson
Executive Vice President -
Marketing & Sales
Burlington Northern Railroad
3700 Continental Plaza
777 Main Street
Fort Worth, Texas 76102-5384

Dear John:

As you know, the Interstate Commerce Commission refused to grant Western Fuels Service Corporation trackage rights in connection with the movement of coal from the Caballo Rojo Mine to Sunflower Electric's Holcomb Station. While we disagree with the ICC's action and have appealed the decision, we see no reason why we should not immediately begin discussions concerning BN's voluntary extension of the trackage rights so requested.

It was interesting to see that in connection with the BN/Santa Fe merger, BN voluntarily granted trackage rights to Southern Pacific, thereby removing SP as an opponent to the merger. This also had the effect -- quite intended I'm sure -- of removing SP from discussions with us about the extension of trackage rights in connection with the Holcomb movement. In addition, SP was a candidate to carry coal over your lines to the Holcomb Station pursuant to the requests that we made there.

While this may be a legitimate business tactic for you to pursue in connection with the merger, it also creates an obligation on your part to voluntarily deal with Western Fuels Service Corporation for the extension of trackage rights to it under similar terms and conditions. It is our view that under applicable Federal law, you are not allowed to discriminate for purposes of maintaining a monopoly position in connection with the relevant coal movement. Stated another way, if you voluntarily agree to grant trackage rights to certain railroads in certain instances, which you quite clearly do, you have an obligation to treat all railroad competitors on similar terms and conditions, including Western Fuels Service Corporation, a Class III common carrier.

405 Urban Street, Suite 305
Lakewood, Colorado 80228
Telephone 303/988-9626
Fax 303/986-8147

4301 Wilson Boulevard, Suite 805
Arlington, VA 22203-1860
Telephone 703/907-6160
Fax 703/907-6161

We, therefore, formally request trackage rights on the Burlington Northern rail line from Denver, Colorado to Sunflower's Holcomb Station for the purpose of creating rail-on-rail competition for the movement of coal in that specific instance.

Time is of the essence for us in connection with this request. Sunflower Electric is paying over market rates for rail transportation services, thus jeopardizing its long term future as a viable, electric generating utility in its relevant market area. This damage to Sunflower, in turn, damages the business of Western Fuels Association since our future as a supplier of coal to the Holcomb Station is likewise jeopardized. Finally, Western Fuels Service Corporation itself desires to be in the rail transportation business to earn money off the movement of coal from Wyoming's Powder River Basin to relevant area electric power plants.

Sincerely yours,

Fredrick D. Palmer

FDP/pc

WESTERN
FUELS
ASSOCIATION
INC.
The National Fuel Supply Cooperative

Fredrick D. Palmer
General Manager and Chief Executive Officer

September 25, 1995

John Q. Anderson
Executive Vice President -
Marketing & Sales
Burlington Northern Railroad
3700 Continental Plaza
777 Main Street
Fort Worth, Texas 76102-5384

Dear John:

As you know, Western Fuels Service Corporation is now a Class III common carrier and is interested in providing rail transportation services. In my travels around the country and in discussions with people that burn Powder River Basin coal, it has become apparent to me that access to rail-on-rail competition for those owning and operating coal mines in the Powder River Basin, those supplying coal supply services focused on the Powder River Basin, and those utilities burning Powder River Basin coal is required if they are to truly succeed in the competitive environment that most of us are operating in.

When the Burlington Northern and the Chicago and North Western agreed to share in the joint line for rail transportation services from coal mines in the area of Gillette, Wyoming, they also entered into a territorial restriction agreement curtailing rail-on-rail competition for mines north of Donkey Creek. Coal mines located in this area are, therefore, disadvantaged relative to coal mines located south of Donkey Creek. Coal brokers selling coal from coal mines located north of Donkey Creek are disadvantaged in competition with those enjoying the benefits of coal sales from coal mines south of Donkey Creek. Electric utilities burning coal from mines north of Donkey Creek that could otherwise secure the services of the Union Pacific are disadvantaged relative to those electric utilities that enjoy rail-on-rail competition south of Donkey Creek.

On behalf of Western Fuels Service Corporation, we are, therefore, requesting trackage rights on the Burlington Northern portion of rail line north of Donkey Creek serving Gillette area coal mines, including our Dry Fork Mine and the Buckskin Mine, owned and operated by Triton Energy. We also, however, would like to serve all the other coal mines similarly situated north of Donkey Creek.

405 Urban Street, Suite *305
Lakewood, Colorado 80228
Telephone 303/988-9626
Fax 303/986-8147

4301 Wilson Boulevard, Suite *805
Arlington, VA 22203-1860
Telephone 703/907-6160
Fax 703/907-6161

John Q. Anderson September 25, 1995
Page 2

We make this request due to two factors:

1. The BN single line is an essential facility for rail transportation services for coal mines north of Donkey Creek;

2. We know there is a business opportunity for WFSC in providing rail transportation services from the BN single line for interchange with either the BN or UP on the joint line.

The Burlington Northern is an active participant in trackage rights markets with other western rail carriers. We noted with interest your granting of trackage rights in connection with the Southern Pacific's opposition to the BN/Santa Fe merger, which effectively removed SP as a potential competitor for the Holcomb Station movement in western Kansas, a power plant owned and operated by one of our members, Sunflower Electric. It is our view that given your voluntary granting of trackage rights to other common carriers, that you are prohibited, by relevant Federal law, from discriminating against Western Fuels Service Corporation in connection with granting trackage rights.

It will be easy enough to establish a fair value for these trackage rights by extrapolation through comparison to the voluntary exchange of trackage rights that you regularly enter into with other railroads. A pro-rata reduction in compensation would seemingly be appropriate in this instance given the relatively short mileage involved and the small amount of investment that the Burlington Northern has in this stretch of track.

We, therefore, request an immediate negotiating session to explore further the rail transportation opportunities that exist on BN track north of Donkey Creek serving coal mines in the area of Gillette, Wyoming.

Sincerely yours,

Fredrick D. Palmer

FDP/pc

BURLINGTON NORTHERN SANTA FE CORPORATION

JOHN Q. ANDERSON
Sr. Vice President
Coal Business Unit
817 333-2001

3700 Continental Plaza
777 Main St.
Fort Worth, Texas 76102-5384
Fax: 817 333-1595

October 16, 1995

Mr. Frederick D. Palmer
General Manager and CEO
Western Fuels Association, Inc.
4301 Wilson Blvd., Suite 805
Arlington, Virginia 22203-1860

Dear Fred:

We received your two letters of September 25, 1995, requesting various trackage rights. While we can certainly understand that "...Western Fuels Service Corporation itself desires to be in the rail transportation business to earn money off the movement of coal from Wyoming's Powder River Basin...." without any investment, (as I am sure hundreds of other Corporations in the United States would), we are not interested in granting trackage rights to any carrier over the routes you described in your letters. Your view that voluntarily granting trackage rights over other rail lines to other common carriers obligates us to grant trackage rights to any specific party over any specific part of our railroad is a novel idea, but certainly not supported by any regulatory requirement of which we are aware. We continue to provide excellent service at competitive rates to utilities throughout the country. The continued burning of BNSF-delivered PRB coal and the continued growth of this fuel at our existing customers' plants demonstrates that we are doing very well for them in a competitive market.

While we have no interest in your proposals for granting trackage rights at this time, we understand your keen interest in this subject and will keep your letters on file and notify you immediately if our interest changes in the future.

Best regards,

John Q. Anderson
Senior Vice President

chh3077

LANGE CO. L.L.C.
101 S 4th, P.O. BOX 520
CONWAY SPRINGS, KS 67031

BEFORE THE SMALL BUSINESS COMMITTEES
OF THE U.S. HOUSE OF REPRESENTATIVES
AND U.S. SENATE
LONGWORTH HOUSE OFFICE BUILDING
NOVEMBER 8, 1995

RE: UP-SP Merger - ICC Finance Docket No. 32760

My name is William F. York, manager of Lange Company LLC, Conway Springs, Kansas. We are a small community in South Central Kansas. We are a receiver of grain, primarily wheat and we ship to a myriad of Grain Terminals and Brokers. We are dependent on Truck and Rail Transportation to move our products to market.

We would much prefer to move grain on rail because we could get our money much faster and therefore costing us less interest on operating money. Our problem is, rail rate are much higher than truck rates from our elevator.

Furthermore, for many, if not all, of our grain movements to out of state locations, trucks are not an effective competitor and we find ourselves with no alternative but to ship by rail. For example, in South Central Kansas this locks our shippers into shipping only to the Gulf market which is not always the best market. We have found that as the railroads continue to merge, our rates continue to increase, not decrease. These high rail rates are seriously eroding our ability to compete.

We presently are located on a shortline railroad operating on leased lines; therefore the rates are set by a large Class I railroad. As Chairman of the UP-MOP Shippers Association in South Central Kansas, our concern is that the proposed merger of the larger railroads will create a duopoly, meaning two large carriers completely dominating

rail transportation in the western United States, and therefore creating a non-competitive environment for shippers to operate in. As mergers continue to happen, our options get less and less. We are therefore stressing the need for additional railroads in the area to keep rates competitive and even allow the possibility of more competitive rates and provide equipment alternatives. We have been told by various shortline railroads that if allowed, they could offer rates that would be very competitive to truck rates, but unfortunately, most of these shortlines connect with only 1 large Class I carrier and thus serve as feeder carriers. As feeder carriers, their traffic and rates depend upon their connecting Class I carriers. Even if there is a shortline that connects with two carriers, for example, UP and SP, as those carriers merge, these shortline and the shippers located on these shortlines lose the ability to benefit from UP and SP competition.

We need Congressional Committees on Small Business to support our small business and country rail shippers in their attempt to remain in business and a part of small town USA. The best way they can do that is by expressing their concern over these rail mega-mergers.

Having been a part of the Grain Industry of 32 years, I have seen disruptive of service resulting from consolidation of railroads into mega conglomerates and the competitive shortline may no longer be present. For example, we understand the UP has informed some Iowa customers of rail service dislocation resulting from the UP-CNW merger. While I am not a lawyer or an economist, if UP and SP are allowed to merge thus reducing the number of railroads in the West from 4 to 2 in less than a year and a half, perhaps there is something wrong with the current merger standards applied by the ICC.

This has been a year like no other in our area as our wheat crop was only a half crop due to the weather and inability to get wheat harvested. When you add this additional expense to our margin, (or lack thereof), we are not able to reduce our transportation costs which creates an atmosphere of business failure.

I would encourage the Congress to do the following:

1. For purposes of filing rate complaints, one must maintain a government agency similar to the Interstate Commerce Commission

2. Allow railroads to arrange reciprocal switching, therefore giving us additional routes to move grain.

3. Encourage the UP-SP to allow the KCS railway to replace the SP rights gained in the BN-ATSF merger proceeding.

4. Revise the current merger standards to focus more on the loss of competition and less upon so-called "efficiency gains" or allow the Department of Justice to review rail mergers as they do for other modes including airlines.

Respectfully Yours,

Chr. UP-MOP Shippers Assn.

SMALL BUSINESS COMMITTEES
OF THE
UNITED STATES HOUSE OF REPRESENTATIVES
AND THE
UNITED STATES SENATE

JOINT HEARING TO EXAMINE SMALL BUSINESS IMPACT
OF RAIL MEGA-MERGERS

STATEMENT OF CONSOLIDATED RAIL CORPORATION

NOVEMBER 7, 1995

Consolidated Rail Corporation ("Conrail") appreciates the opportunity to submit this statement before the Small Business Committees of the United States Senate and House of Representatives. Conrail, a Class I rail carrier, was created in 1976 after the collapse of six bankrupt freight carriers in the Northeast and Midwest. It stands as a unique success story, having survived and re-entered the private sector as a profitable carrier. It accomplished this feat by close attention to costs, significant productivity improvements, and attention to market-driven customer needs. With that perspective, Conrail shares the concerns of small shippers -- indeed all shippers -- over the trend toward "mega-mergers" and hopes that the Committee will look closely at the effect such developments could have upon competition for the nation's freight business.

In particular, currently pending before the Interstate Commerce Commission is the proposed merger of the Union Pacific (with its

affiliates)("UP") and the Southern Pacific Railroad (and its affiliates) ("SP"). This merger has raised concerns in many shippers' minds, primarily about the loss of competitive rail options in many markets that were served by both the UP and SP, including those involving traffic moving to and from Mexico and the Gulf region. For the Committee's convenience, attached are maps that show the combined UP-SP system and the two major western railroad systems -- UP/SP and BN/Santa Fe after the completion of both mergers. (BN/SF has been approved; UP/SP has not yet been reviewed.)

The alarm over this merger was sounded early, when the UP/SP proposed a procedural schedule for review of this transaction of 195 days -- only six months. The Commission itself proposed an even shorter schedule. These foreshortened timeframes were attacked not only by shipper interests, but by a broad coalition of government, labor, shipper, and railroad interests concerned that little considered thought could possibly be invested in the context of this enormously complex and significant proceeding by the affected parties or the Commission in so short a period. Moreover, these interests identified significant competitive concerns. While UP/SP proposed a hastily written agreement with the Burlington Northern/Santa Fe system primarily relying on trackage rights as solving all of the competitive problems, it was obvious that such an important conclusion cannot be reached in so abbreviated a time frame. Even the Commission's final procedural schedule -- 255 days -- may be inadequate.

UP/SP's trackage rights proposal has itself been received critically by the shipping community, and for good reason. Many shippers have, bluntly, stated that trackage rights pose operating problems. (Trackage rights are rights held by one carrier (the tenant) to operate its own trains on the lines of another carrier (the owner)). Customers are concerned that the owning railroad has considerable power over the tenant's ability to offer competitive service both with respect to price and with respect to the timing, speed, and flexibility of service. In fact, SP accused UP of these very practices only a year ago in UP's merger case with the Chicago and North Western Railroad. Shippers are also concerned that the tenant may lack incentives to invest in the lines or the ability to work with customers and local communities to bring new business to the lines (thereby assuring their future viability and the presence of as many customers as possible to share the costs). The tenant may be required to operate lines far away from its central base; or it might be operating over lines that are, themselves, second-class. And, of course, operating problems that break down service to large shippers can destroy service schedules for small ones.

These issues must be addressed carefully and fully in order to determine whether the trackage rights proposed by UP/SP will supply the kind of vigorous and effective competition that can serve both the large and the small shippers in the affected areas of the country, including Texas, Arkansas, and Louisiana.

Moreover, several railroads have made offers to alleviate the competitive problems with the merger and those options have yet to be considered. In

addition to proposals given wide publicity from the Kansas City Southern Railway, the Illinois Central railroad, and the South Orient Railroad Company Conrail has made public the fact and substance of its very substantial offer to UP to purchase:

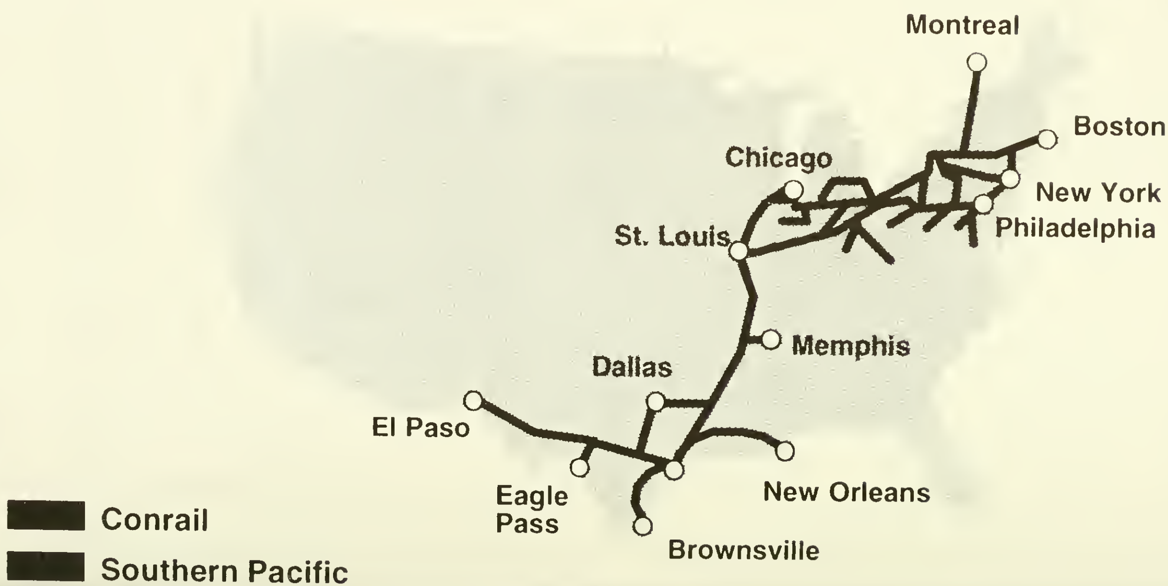
- SP lines extending from Chicago to Galveston TX and Brownsville, TX;
- SP lines extending from New Orleans, LA to Spofford, TX, Eagle Pass, TX and El Paso, TX and all intermediate Texas points;
- connecting track serving Alton, IL, New Madrid, MO, Memphis, TN, Little Rock, AK, Indiana, AK, and Breaux Bridge, LA;
- ownership interests in connecting subsidiaries in St. Louis, Houston, and elsewhere; and
- cars, locomotives and other equipment necessary to facilitate service.

Also attached to this statement is a map that shows the combined Conrail- SP-East system were Conrail able to purchase it. While UP rejected this offer without negotiation, Conrail has made known its willingness to keep its offer on the table and to pursue it if the affected customers support it.

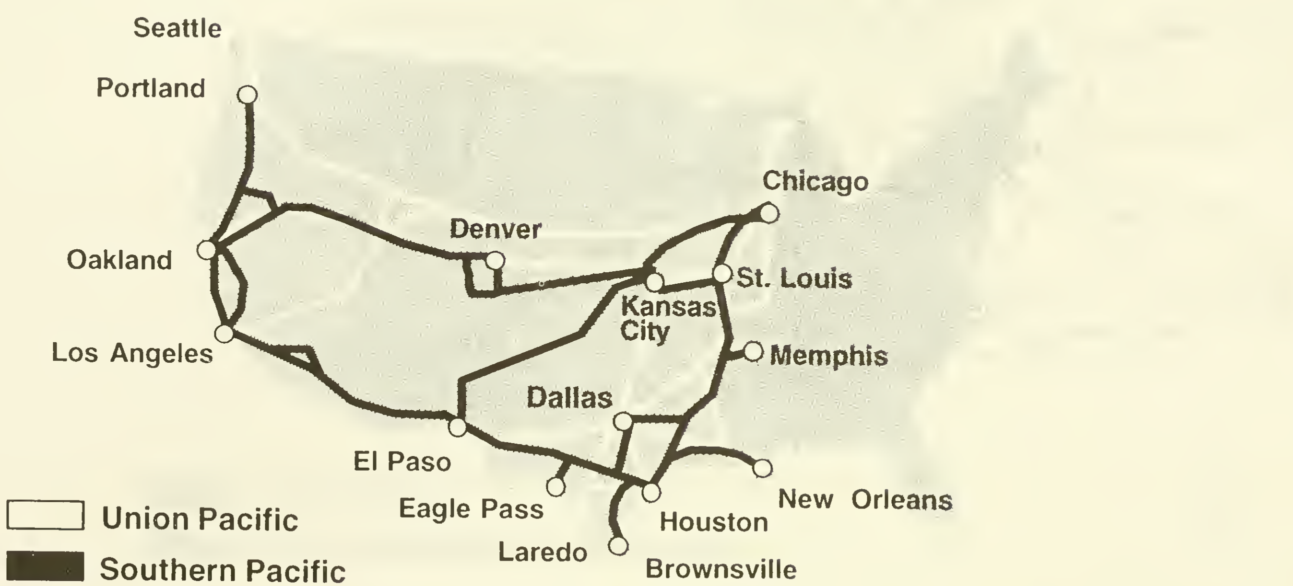
The clear and widespread alarm over the competitive problems with the UP/SP merger, and the myriad available options to address those concerns, all suggest that this particular merger deserves the utmost scrutiny by all parties -- both the ICC (of course, which has jurisdiction to approve it) and the Congressional interests whose constituents could be adversely affected -- and the time to review it. Conrail stands ready to supply you with any information you

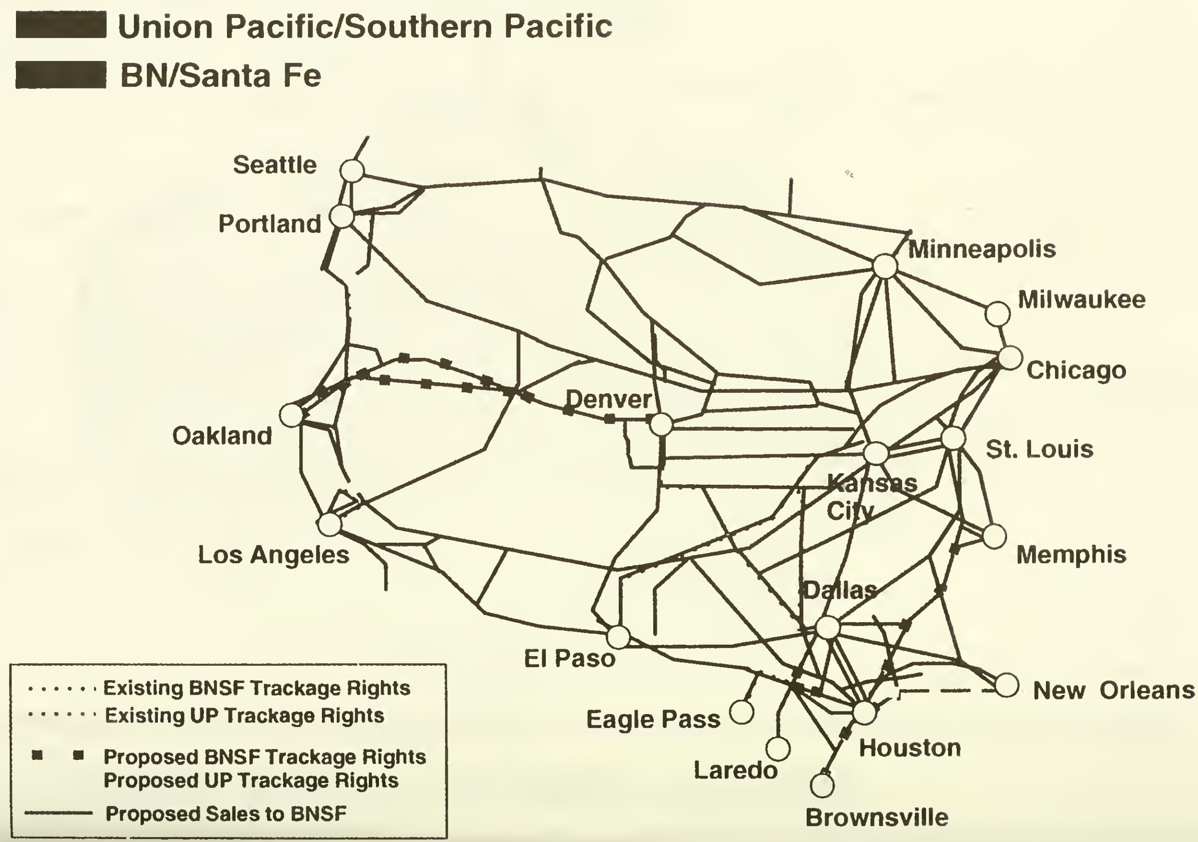
need about its proposal and how it would cure the competitive problems our customers say are presented by the UP/SP proposal.

Conrail/SP East



Union Pacific/Southern Pacific




Union Pacific/Southern Pacific
BN/Santa Fe
Seattle
Portland
Oakland
Los Angeles
Denver
Minneapolis
Milwaukee
Chicago
St. Louis
Kansas City
Memphis
Dallas
El Paso
Eagle Pass
Laredo
Houston
Brownsville
New Orleans
Existing BNSF Trackage Rights
Existing UP Trackage Rights
Proposed BNSF Trackage Rights
Proposed UP Trackage Rights
Proposed Sales to BNSF

FLETCHER GRAIN COMPANY
· MARSHALL ·
MALTA BEND · BLACKBURN

Fletcher Grain Company, Inc.

P. O. Box 776
Marshall, Missouri 65340
816-886-6976

Senator Kit Bond, Senator from Missouri
293 Russell Senate Office Building
Washington, DC 20510

Attn: Keith Cole
FAX: 202 224 8149

November 2, 1995

Dear Sir:

I understand that Senator Bond and Representative Meyers will hold hearings to examine the impact to small business of the class one rail carrier mergers. I am very interested in this subject and have particular concerns about the merger between the Union Pacific and the Southern Pacific. I also have strong concerns about the legislation that is being "railroaded" through the House of Representatives.

Rail lines such as Southern Pacific and Kansas City Southern have do not have strong origination points for feed grains that are needed by destinations that they serve in the southwest. They have been dependant on other lines to provide that origination. Railroads such as ATSF, GWWR, NS, and UP have provided the origin location and delivered freight to interchange cities, such as Kansas City. From there the carrier that serves the receiver takes the freight and delivers it.

In cases where the UP is both the origin carrier and the destination carrier, there are concessions in the freight rates from the origin to the interchange city. UP publishes lower rates from an origin to the interchange city if the movement is for beyond that city than if the city is the termination for the move. For example, the rate from Marshall Mo to Kansas City for a car that terminates in Kansas City is $600.00 per car. If the same car is shipped from Marshall MO to Kansas City, for continued movement to west Texas or Arkansas, the rate is $470.00 per car. This encourages cars to stay on one rail line most of the time and contributes to better car management by the railroads.

Railroads that do not have adequate origination capacity must rely on other lines such as Gateway Western or Norfolk Southern. These railroads in the past have solved their lack of origination in one of several ways. Sometimes they have offered lower rates to comparable destinations from the interchange city. This has allowed the origination carrier to obtain sufficient revenue for the first leg of the move and make the entire movement remain cost competitive. Other times they have passed back revenue to the origin carrier, so the origin carrier could offer a rate that is competitive with the origination rates offered

by UP. Still other times the market itself has priced grain bound for destinations on the SP or KCS at a premium to UP destinations.

Concessions made during the BN-ATSF merger would have created even stronger demand for SP destination grain. Many ATSF destinations in Texas will also become SP destinations because of anti-competitive concerns raised during that merger. This will make feeder markets available to grain shippers who are served by lines that do not reach those markets. Non ATSF origin grain would have moved into markets that had been traditionally locked by ATSF. Because SP does not have adequate origination capacity in the corn belt, much of that grain would have come from origins on other rail lines. The proposed merger will essentially lock up those destinations for UP origins, denying competitive access that exists today to those markets by other railroads. This will eliminate the benefits of the of the BN-ATSF merger concessions.

My concerns about HR2539 are rooted in the same concepts. The western railroads were built in this country as a public convenience. The construction of the roads was paid for by the citizens of the United States. In the case of the Union Pacific, the citizens of the United States paid for it again by reviving it from bankruptcy in the 1880's It paid for it again during World War I when the neglected roads were nationalized and rebuilt for the war effort, and then after the war were given back to the owners of the UP.

It is hard to believe that the US government can look at a company such as Microsoft and see a monopoly, and look at the railroads and not see a monopoly. The typical response from the railroads is that they have competition from trucks and barges. In certain markets this is true. But trucks and barges serve a certain need for industry while rail carriers serve another need. In areas where trucks and barges are an acceptable alternative, there is competition between truck lines and barge lines. To tell a grain shipper in Nebraska or the Dakotas or a grain receiver in west Texas that trucks are legitimate competition is like AT&T telling a long distance telephone user to "send a letter" prior to telephone de-regulation.

Please don't miss read my intentions. I do not oppose deregulation. The deregulation of the airlines has resulted in increased competition and more competitive rates. The same applies to truck freight. The same applies to long distance telephone service. In the 1980's immediately after the Staggers act was passed, prices for rail service came down. But in 1980 there were over twenty class one railroads competing for business. Today there are seven, and two of them are in the process of merging. Another (the IC) is but a shell of the railroad it was in 1980. Since 1990, prices have risen steadily in the rail sector, while trucks have remained competitive. During this time railroad earnings are also experiancing significant growth. At the same time the class one carriers have steadily made access to their services more difficult. The Union Pacific is telling shippers that if they cannot ship 100 cars at a time they will not be able to use their service.

The purpose of the legislative efforts by the railroads in Congress is to reduce the level of competition. HR 2539 eliminates the requirement for reciprocal switching. Reciprocal switching allows a shipper in a city that is served by competing rail carriers to ship on a

carrier that his facility is not physically upon. It allows the two carriers to compete for business. What purpose would elimination of reciprocal switching serve, except to eliminate competition.

The bill would eliminate the tariff filing requirement. For talking purposes, let us concede that barges and trucks are legitimate competition for rail. With each of those forms of transportation, a shipper has the ability to know what his cost will be when he arranges for the transportation. Under this legislation the shipper conceivably could order the cars, then see the price increase after he receives the cars, and have to pay a penalty for canceling the car order.

Rail carriers do operate monopolies in most of country and until Congress can provide for legitimate competition among railroads, Congress should allow protection to the public as is provided to the public from other public utilities.

If you have questions about my position on this matter I can be reached at 816 886 6976.

Sincerely,

John Fletcher

U. S. Department of Justice

Office of Legislative Affairs

Office of the Assistant Attorney General

Washington, D.C. 20530

November 10, 1995

The Honorable Christopher S. Bond
Chairman
Committee on Small Business
United States Senate
Washington, DC 20510

Dear Mr. Chairman:

The Department of Justice has been informed that the Senate and House Committees on Small Business held a joint hearing on November 8th on the impact of rail consolidation on small shippers, with a particular emphasis on the impact of mergers involving Class I railroads and how such mergers should be reviewed at the Federal level to ensure that competitive rail services can be maintained for the small shippers who depend upon them.

Your committee should be congratulated for its interest in this important subject. Maintaining competitive market structures in all of our infrastructure industries, including telecommunications, electric power, and a variety of transportation services, is vital to ensuring competitive opportunities for producers of other goods and services, and vital to maintaining low prices and ample product choices for consumers.

This letter is to provide the views of the Department of Justice on this important subject, particularly on the issue of how rail mergers should be reviewed in the future. We ask that this letter be included in the record of your hearing.

In brief, the Department believes that railroad mergers should be reviewed under the same legal standards that apply to virtually every other sector of our nation's economy. The specialized provisions for reviewing mergers under the Interstate Commerce Act (ICA) should be repealed, and rail mergers should be subject to the antitrust laws and reviewed by the Department of Justice.

This has been a long-standing position of this Administration, as reflected most recently in the Department of Transportation's Report on the Functions of the Interstate Commerce Commission (July 1995). This approach to rail mergers is the one best calculated to maintain competitive rail services

for small shippers and, indeed, all users of rail services in the United States.

Review of Mergers at the Department of Justice

The Department of Justice reviews mergers under section 7 of the Clayton Act, 15 U.S.C. Section 18, where the central issue is whether the merger will result in increased prices to consumers or reduced services. Under the premerger notification provision of the Hart-Scott-Rodino ("HSR") Act, 15 U.S.C. section 18(a), routine mergers that raise no antitrust issues can be consummated upon the expiration of a 30-day waiting period.

Where a merger may raise antitrust concerns, we possess the necessary discovery and investigative tools needed to obtain all of the information we need to resolve those concerns effectively and efficiently. The Department gathers information from competitors, suppliers, customers, employees, and other knowledgeable parties in order to analyze the effects of the merger.

When the Department determines that a proposed merger does raise significant competitive issues, several steps are available to resolve the matter in a comparatively short time. The parties can "fix-it-first" by restructuring the transaction, which avoids a legal challenge by the Department. If the investigation runs its course and the Department decides to challenge the transaction, the parties and the Department frequently negotiate a consent judgment that corrects the competitive problem, but otherwise allows the remainder of the transaction to go forward. Consent decrees resolving cases are subject to an open "public interest" review under the Tunney Act, 15 U.S.C. § 16. If the Department concludes that a merger transaction, as structured, would violate the antitrust laws, and the parties do not wish to restructure it, the Department must go to court to prevent the transaction. Only a small percentage of the mergers reviewed by the Department are challenged in court, however.

The analytical framework we use in merger investigations is set forth in the 1992 Horizontal Merger Guidelines, issued jointly by the Department of Justice and the Federal Trade Commission. These Merger Guidelines have been cited and relied upon by the court in merger cases. Under the Merger Guidelines, we assess the merger's likely harm to competition, and consider any efficiencies that may outweigh potential harmful effects. The antitrust laws do not prohibit efficient railroad mergers that can benefit shippers. Thus, the Department of Justice will challenge a merger only when its likely harm to competition is not outweighed by its likely efficiencies.

ICC Sunset Legislation

It is for these reasons that we have grave concerns about H.R. 2539, the ICC Termination Act of 1995, which has recently been ordered reported, as amended, by the House Committee on Transportation and Infrastructure. Unlike the Administration's ICC sunset proposal (introduced as H.R. 1436), this legislation would retain most of the current, outmoded economic regulation of the trucking and railroad industry and unwarranted exemptions from the antitrust laws, and simply transfer the regulatory function to a new "Transportation Adjudication Panel" within the Department of Transportation. This approach is inconsistent with the goals of deregulating these industries and with sunsetting the ICC.

The Department of Justice possesses the experience and expertise to evaluate future rail mergers efficiently, quickly and thoroughly, using a proven competition standard capable of distinguishing between proposals or procompetitive mergers that would improve rail transportation, and those that should be opposed or modified. The Department has always been a party of record in ICC proceedings that concerned potentially anticompetitive rail mergers. This experience, in combination with the Department's extensive experience in analyzing mergers generally, both within and outside the transportation industry, is a strong justification for the Administration's proposal to transfer ICC merger review authority to the Department of Justice.

There is no evidence that applications of an antitrust standard of review in other regulated industries, such as electric power and telecommunications, has in any way harmed legitimate producer or consumer interest, or that procompetitive transactions are discouraged by the application of an antitrust standard of review. As a result, we see little justification for the proposal in H.R. 2539 to provide immunity from private suits for rail mergers approved by the government.

Lessons learned from the experience of the airline industry are particularly illustrative. The Department of Justice now reviews airline mergers under traditional antitrust standards and airline mergers receive no immunity from suit after review by the Department of Justice. There is no evidence to suggest that this has injured the public interest or hindered procompetitive transactions.

In sum, our analysis of proposed rail mergers using the Merger Guidelines is the same general analysis we use in reviewing mergers subject to the antitrust laws generally. That analysis is sophisticated, thorough, and flexible -- it involves far more than simply computing market shares or concentration figures. It takes into account all the dynamics of the markets

with which we are dealing. Subjecting railroad mergers and acquisitions to the antitrust laws administered by the Department of Justice would expedite both the investigation and resolution of such transaction. Significantly, for the purposes of your hearing, it would also benefit shippers.

We hope these comments are helpful. Again, we would appreciate it if you could include this letter in the record of your hearing.

The Office of Management and Budget has advised that there is no objection from the standpoint of the Administration's program to the presentation of this report.

Sincerely,

Andrew Fois For A.F.
Assistant Attorney General

To The
Senate Committee on Small Business

Statement
of
Willard Garvey
on behalf of
Garvey Industries, Inc.
(316) 261-5396, FAX (316) 262-5101

My name is Willard Garvey. I am Chairman and President of Garvey Industries, Inc., located at 300 W. Douglas, Wichita, Kansas 67202. For several decades I have served as CEO of the businesses and operations of Garvey Industries, Inc. and our subsidiaries.

I appreciate this opportunity to submit a statement concerning the benefits that mergers can bring to small businesses. I wish to discuss in particular my perspective on the many benefits for small businesses that I see arising from the proposed merger of Union Pacific Railroad ("UP") and Southern Pacific Railroad ("SP").

Over the years, my company and its various subsidiaries and affiliates have been involved in a wide variety of businesses that depend on efficient railroad service in order to be profitable and remain competitive. Among those businesses are farming, ranching, grain storage, grain merchandising, milling, pelleting, food processing, short line railroads, railroad car leasing, tug boat and barge operations, warehousing and other operations.

For example, we ship Kansas and other Midwestern farmers' grains to various points throughout the United States, both for domestic consumption and for export. Particularly important destinations include Southern California, Arizona, Texas, the Gulf Coast ports generally, and border crossings to Mexico.

Overall, we believe that the proposed merger of Union Pacific and Southern Pacific would be in the best interest of our company and small businesses in general. Efficient and reliable service is important to small businesses to avoid lengthy delays in the delivery of and payment for their goods. To remain competitive, they rely increasingly on just-in-time delivery to avoid storage costs and to minimize inventory carrying costs. In addition, grain shippers must be able to reach a wide variety of markets as economically as possible. Combining the systems of UP and SP would create a stronger, more efficient railroad, capable of reaching more markets and competing with the newly merged Burlington Northern Railroad Company and The Atchison Topeka & Santa Fe Railway (now Burlington Northern Santa Fe) in order to maintain vigorous rail competition in the West.

First, a fundamental benefit of the proposed combination of UP and SP would be the creation of many more efficient, single-carrier routes for shippers from the Midwest and other regions. Shippers now served by UP will be able to reach many new SP served points

for the first time without an intermediate interchange to a separate carrier, and SP shippers will have new opportunities for single-line service to UP destinations. Single-line service has been roundly recognized by shippers and the interstate Commerce Commission as more efficient and economical than joint-line service. By eliminating the need for intermediate handling, shipments move faster, costs and damage are reduced, and reliability is improved. Shippers also benefit by having to deal with only a single carrier for pricing and customer service. This increases responsiveness and makes it easier to track the progress of shipments and anticipate and resolve service issues. By expanding available single-line service, the merger will create new market opportunities for Midwestern shippers.

New single line service opportunities could be particularly significant for shippers to Mexico. The merged system would have improved single-line routes and full access to all major Mexican border crossings. This would create added flexibility for export shippers, and allow them to take full advantage of growing Mexican markets and different transportation options South of the border.

There would also be improvements over many specific routes. Shippers at SP origins would have a new single-line route over UP's more direct lines South to the Gulf. This would give many exclusively served SP shippers a viable outlet to export markets through Gulf ports for the first time. Shippers at UP-served origins would be able to use SP's Tucumcari line in a single-line service for a more direct connection to the Southwest. This would allow them to compete more effectively in the large feed stock businesses in Arizona and Southern California. Movements west will also receive more efficient service using the combined routes of UP and SP over the central corridor. With the increased volumes that come from combining traffic, UP/SP would be able to separate much of their high speed, priority intermodal traffic from their manifest (carload) traffic moving over the central corridor. This traffic separation would help reduce congestion and reduce transit times for both types of traffic. In addition, the combined system would be able to realign traffic between Salt Lake City and Ogden, Utah, to significantly reduce delays.

Second, in addition to single-line efficiencies, combining the routes, facilities, and traffic of UP and SP will create a more efficient carrier with fewer bottlenecks. By joining facilities of UP and SP at congested terminals, such as Kansas City and Houston, congestion will be reduced. Further, with greater volumes, additional pre-blocking of traffic will be possible, allowing shipments to avoid congested yards altogether.

Third, the merger would also allow UP and SP to combine and jointly manage their locomotives and freight cars. This should go a long way toward ending the severe equipment shortages SP has suffered over the past several years, and the freight car shortages that have long been a concern of midwestern grain and other shippers. By combinlng their equipment and routes, the new UP/SP will be able to manage its fleets more effectively, taking advantage of differences in shippers' peak growing seasons, increasing opportunities to triangulate traffic movements and create loaded backhauls. the more efficient management made possible by the proposed merger would allow UP/SP

added incremental loaded service miles from each of their cars, in effect increasing the capacity of their joint fleet.

Fourth, important service benefits are also expected to follow from UP's ability to finance improvements in SP's system. SP has suffered from cash shortages for several years. As a result, it has been forced to postpone worthwhile capital projects that would significantly improve service over its lines. SP yards such as Roseville and West Colton are in need of rehabilitation and expansion, and SP's Tucumcari line and its route between El Paso and W. Colton require upgrading and capacity increases to reduce congestion. I understand that UP, with its greater financial resources, plans to make these improvements. The result will be faster, more consistent service over these important SP routes to the benefit of shippers generally, including Kansas, Missouri, and Iowa elevators and farmers, for movements to California and the Southwest.

Fifth, it is important to also note that the benefits of this merger are not limited to SP and UP shippers. Burlington Northern Santa Fe (BNSF) shippers will gain new service options as a result of a settlement agreement entered into between UP/SP and BNSF that provides unprecedented new rights for both these systems. That agreement is precisely the type of pro-competitive private agreement that Congress and the Federal government should applaud. Among other things, that settlement agreement provides a new central corridor route for BNSF from Denver to the West Coast, a new direct single-line route from the Pacific Northwest to California, and a new route for BNSF between Houston and Memphis. It also provides BNSF with new trackage rights to the border crossings of Eagle Pass and Brownsville, and access to Laredo, the most widely used border crossing, through a new connection to Texas Mexican Railway at Corpus Christi. These new rights to Mexican border crossings and the new central corridor route of BNSF should benefit Midwestern grain shippers served by BNSF that export to Mexico or ship to the West Coast.

Another important benefit for BNSF shippers would be the creation under the settlement of new competitive pricing authority for UP/SP from BNSF-served points in the Pacific Northwest, including Vancouver, for shipments to California and the Southwest. This new pricing authority would create rate competition for movements from these BNSF points for the first time. These rights would complement the improved single-line service over the so-called I-5 corridor (from the Pacific Northwest to California) that would result from the proposed merger.

The settlement agreement between UP-SP and BNSF also holds benefits for UP/SP shippers. Importantly, it provides BNSF with access to every single shipper that receives rail service today only by SP and UP. By doing so, it ensures that no shipper would lose its sole competitive option by reason of the proposed UP-SP merger. To the contrary, shippers currently receiving rail service only from SP and UP would now have access to what is currently the largest, most powerful rail carrier in the U.S. This competitive solution is far superior to providing access to a weaker competitor at these points. In addition to resolving any competitive concerns at locations jointly served solely by UP and SP, the settlement agreement includes important trackage rights grants from BNSF to UP/SP in

California and Oregon. These rights will improve service to shippers in Eastern Oregon and Washington, and allow the combined UP/SP to use equipment more efficiently.

For anyone harboring any doubts about the pro-competitive nature of the proposed UP-SP merger, the foregoing should firmly tip the balance in favor of approval.

A sixth issue I would like to address is the importance of this proposed merger to maintaining and strengthening rail competition in the West. This is a critical issue to small businesses that rely on railroads to source inputs and reach markets. Too often, when competition among service providers is reduced, it is the small businessman that suffers due to his or her lack of market clout.

In this case, the proposed merger is strongly pro-competitive. Not only are shippers served exclusively today by UP and SP protected as a result of the BNSF settlement agreement I have described, but other shippers will benefit from the creation of a new UP/SP with the financial strength and routing capabilities necessary to provide an effective counterbalance to the recently created BNSF system. Neither UP nor SP is adequately equipped by itself to compete over the long-term with the much larger and stronger BNSF. We would much rather have an equal competitor available than two small and weaker competitors that are unable individually to provide the efficient, competitive service they can provide as one. SP in particular, because of its continued inability to invest adequately in its future, appears to be in danger of becoming at best a marginal competitor. Combining UP's financial strength, and SP's strong route structure, will assure that vigorous rail competition is preserved in the West.

Finally, I think these two railroads should be allowed to merge and your committee should give competitive enterprise and a free market full rein. As you probably know, regulation is counterproductive -- a major obstacle to small business and the overwhelming burden to the citizen/consumer. Are you aware Government more than doubles -- probably triples -- each citizen's cost of living? For small business, competition, innovation, technology and the economic self interest of each player will insure quality service -- lower costs and customer satisfaction -- better than government intrusion. Small business can use alternate sources of transportation, revise its product, or use other markets. For railroads, competition requires quality rail service -- competitive pricing. Railroads desire to grow customers -- not price services out of the market -- thus damaging its customers and losing rail business.

The only permanent monopolies are those sanctioned by government, do you agree? A free market system, competition and technology restore temporary imbalances, if any, sooner and better than government. While regulation may appear to protect certain businesses and citizens short-term, regulation long-term invariably adds increased costs to the consumer. These taxes, inflation and opportunity costs outweigh any real or imagined short-term benefits. For our country to excel competitively, isn't a first priority to reduce government spending and intrusion?

Thank you for providing me this opportunity to make my views known to the Committee. I hope you will consider them in examining the broader issue of merger effects on small businesses.

Willard Garvey
8 Nov '95

SKILL TRANSPORTATION CONSULTING, INC.

1809 N. BROADWAY, SUITE H, WICHITA, KANSAS 67214 (316) 264-9630

November 15, 1995

Christopher S. Kit Bond
c/o Senator Kit Bond
Keith Cole
428 A. Russell Bldg..
Washington, D.C. 20510

RE: Small Business Committee Meeting Joint Hearing Nov. 8th. Skill's Written Statement.

Honorable Senator,

It was a memorable trip to Washington to attend the Nov. 8th Joint Committee Hearing on Mega Mergers. Bill York, who testified for the Kansas Shippers Group and I caught an early 6:00 a.m. flight and returned to Wichita at 10:30 p.m. Both of us are mature individuals and work for small businesses.

I attended the meeting to receive information which would be helpful for my written statement. Needless to say, it was one of the better conducted hearings which I have attended in my 40 years of Transportation experience. I've included the statement of Larry Coffman which portrays an interesting development of an ICC case, federal court proceeding, 10 years of fighting alone with a mega carrier, Bankrupting a Coop and ill health to Coffman. It illustrates the reason why small businesses have to be protected in todays mega carrier environment.

Respectfully yours,

Jim Irlandi
James J. Irlandi
President

JJI/sl

BEFORE THE SMALL BUSINESS COMMITTEES
OF THE U.S. HOUSE OF REPRESENTATIVES
AND U.S. SENATE
RAYBURN HOUSE OFFICE BUILDING
NOVEMBER 8, 1995

RE: UP-SP Merger - ICC Finance Docket No. 32760

My name is James J. Irlandi and I am President of Skill Transportation Consulting, Inc., with offices located at 1809 N. Broadway/Suite F, Wichita, Kansas 67214. Our telephone and fax numbers are 316-264-9630 and 316-264-9735.

Skill is an advisor to the Kansas Shippers Association which is comprised of the UP-MP, SFE, and SSW Shippers Groups. A total of 36 companies are shippers/receivers of agricultural products, lumber, cement and plastics.

Please refer to Appendix A-1 for my transportation employment and experience. In addition, Appendix A-2 is a listing of the shipper clients and the railroads serving their numerous facilities. A shipper may have all facilities on one railroad, or in the alternative on two or three railroads.

STATEMENT OF INTEREST

As an advisor to the Kansas Shippers Association, I attended the meeting held on November 8, 1995, in order to receive information from the Panel and witnesses for the preparation of this statement. The information I received gave impetus to research the files in order to help the Panel understand **the scope of Kansas shippers' betrayal by the railroad mega carriers**. The railroads' guise of increased efficiency, better service and technological advances in railroading is offset with higher freight rates, poor service and no equipment to be furnished to small businesses.

BACKGROUND INFORMATION

Skill Transportation learned of the proposed merger from magazines, newspapers and other periodicals. Members of the Kansas Shippers Association were not contacted by either the UP or SP Railroads concerning the proposed merger. This followed the same pattern established in the BN-ATSF merger procedure. In fact, it is my understanding that our two train loading members did not receive any **advanced information** of the proposed UP-SP merger. Since several of our members have given both the UP and SP Railroads thousands of cars of business in the past, we believe this neglect demonstrates the attitude of the UP and SP officials.

MAJORITY OF DIRECTORS VOTED TO OPPOSE THE MERGER

Skill conducted a blind vote, as well as a meeting and phone survey to determine the posture of these three shipper associations. All but the two Train Loading Directors voted to oppose the merger. Both of these directors abstained from voting. The majority of directors voted to oppose the merger for the following reasons:

1. **They were not contacted by either railroad in advance of public announcement.**
2. **They felt betrayed by the SP, as does Skill Transportation's President, for working so hard and diligently to have the SP serve Kansas with operating rights granted in the BN-ATSF merger.**
3. **They felt betrayed once again by the announcement that the UP and SP granted trackage rights to the BN-ATSF railroads without any previous announcement.**
4. **Many shippers on the SSW railroad do not like the UP car-ordering system.**
5. **Shippers on the main lines are fearful of losing local service as well as equipment procurement.**
6. **Mega carrier mergers are harmful to short line railroads and their shippers.**
7. **The loss of the SP railroad service in a short time frame is harmful to small businesses unless replaced by another Class I carrier, namely one which is headquartered close to Kansas.**

All of these issues will be treated infra (below)!

COMPETITION CRUCIAL TO MEMBERS

This increased concentration of the rail industry in Kansas and specifically, the combination of carriers (BNSF and UP-SP), which serve our area by direct and joint line service reduces the ability of the majority of the members of the Association to obtain competitive rail rates and service. The availability of competitive options is crucial to most of the members in obtaining competitive rail rates, service, and railroad equipment.

BETRAYAL BY OFFICIALS OF THE UP-SP RAILROADS

Our members were concerned with the BN-ATSF merger. Meetings were held to discuss the need of an additional Class I carrier to serve the Hutchinson, Wichita, and Winfield areas in what was named the Kansas City to Fort Worth Corridor. Their advisor, (Skill Transportation), was informed of the Directors' vote which was unanimous to contact the SP Railroad for help.

Affidavits were prepared for the SP Railroad which were mailed to Denver to be included with the SP Railroad protest for furthering to the ICC.

Conversations were held with the merger teams who were preparing to come to Kansas. The first merger team consisted of two SP officials who were scheduled to meet with the Kansas Governors' Rail Working Group on April 7, 1995, at Topeka, Kansas. The team members were Kenneth Bosanko, Managing Director of Strategic Planning, and an attorney whose name escapes me at this time. Kansas Shippers Association was represented by Jim Irlandi at that meeting. He delivered a strong statement in support with the attachments, including copies of all affidavits submitted to the SP's Denver office.

Director Bosanko and the attorney were a very capable team and dedicated employees of the SP Railroad. It appeared that both had no knowledge of the proposed UP-SP merger. Skill's President, Jim Irlandi, received a letter from Denver, Colorado dated May 1, 1995, authored by Peter J. Rickerhauser and generally stating, "Thank you for writing a verified statement to the ICC in support of SP's requested conditions to preserve and enhance competition in light of the proposed BN-ATSF merger." The letter outlined the SP's gain. In addition, SP gave away trackage rights to the BN-ATSF which caused us to question, "What's going on here?" The letter also stated:

"As a result of the successful negotiations, Southern Pacific will not be filing a volume of verified shipper support statements with the Interstate Commerce Commission. The verified statement that we received from you is enclosed."

Thank goodness we had the foresight to send copies of our affidavits to the U. S. Department of Transportation and the Department of Justice. The ICC never received this vital evidence of the need for additional competition. We were again perplexed! It became apparent why at a later date.

Skill's President met with the operating team of the SP to help develop information on the switching district of Wichita. This team consisted of Susan Fox, E. L. "Buck" Hord, and R. L. Dick Fields, Director of Short Line Relations. Skill's President also attended a meeting with the WTA switching railroad and furnished tariff switching information as well as a blueprint of the WTA'S switching district.

Additional help was rendered to the SP in the above case, Docket 32549, by supplying additional comments concerning open access for the short line railroads. After the SP agreement with the BN-ATSF was announced, we again became doubtful of the help rendered to the SP railroad. Why would the SP give up trackage rights between El Paso and Topeka? Give up access to all industries at Liberal and McPherson, Kansas, and Hooker and Guymon, Oklahoma? Interchange with other carriers to be permitted out of El Paso, Hutchinson, Vaughn , New

Mexico, Stratford and Dalhart, Texas. Additional haulage rights between Caldwell and Eagle Pass, Texas. The UP was only asking for trackage rights between Abilene, Kansas to Superior, Nebraska. It became obvious after handling several merger proceedings and discussing the issue with other Kansas transportation officials that something was "Radically Wrong."

USDOT RECOGNIZES NEED FOR COMPETITION

The brief of U. S. Department of Transportation in Finance Docket No. 32549 (the BN-ATSF merger case) recognized the need for additional competition in the Kansas City - Fort Worth Corridor. Even though it was a redacted version, pages 13 and 14 thereof supported our needs for competition. Specifically, paragraph c-- the area around Wichita, Kansas. In order to support our contention that the KCS Railway is desperately needed, we are attaching copies of pages 13 and 14 for support of our posture.

Betrayal came faster than anticipated. It was the granting to the BNSF Railroad operating rights which should have been granted to other Class I carriers. Skill's President, who opened the door for the SP employees gave them all the help possible, and furnished important material to them also considered the BNSF railroad grants a "Betrayal of Trust."

CONCERNS OF SERVICE AND CAR SUPPLY

As an advisor and consultant to these shippers, it is apparent to me that future UP-SP emphasis of main line and single line service will preclude service to the majority of the member shippers. Past experience with the UP has shown a curtailment of service on main lines to local shippers, giving preference to through train traffic to the exclusion of local originations and termination. Some shippers on KSW have waited more than a month for UP cars to be used in loading to destinations beyond the junction point at Wichita with UP.

This concern may vividly be expressed by a recent letter from the UP's new President Rob Burns to Iowa and other UP grain customers. It stated:

> **"Many customers are experiencing unprecedented problems with service provided by our Railroad. I assure you that this critical situation has the utmost attention of all of us at Union Pacific.**
>
> **While we don't have all the answers yet, we know where to focus our efforts. With power already tight and line capacity strained across our system, we knew that implementation of the Chicago & North Western (C&NW) would be a challenge. Indeed, the learning curve on the cut over has been steep, and there have been some operations and systems slips along the way. As a result, service has deteriorated to levels never before on UP. So here's what we are doing about it:**

We are leasing every locomotive we can find from any source in the U.S. and Canada, including Amtrak. So far, we've increased our fleet by 137 leased units, and we're adding another 120 units by the middle of February.

During September and October, we recruited and hired more than 200 new train crew employees. This is in addition to more than 660 train and engine employees hired since the beginning of the year.

To take advantage of the additional power and train crews, we are implementing a new operation plan designed to balance our locomotive power and crews, minimize main line congestion, and improve flow through terminals.

An additional operating region is being assigned to better manage daily operations. We are also putting more people into the field to handle your business.

We plan to work throughout the Thanksgiving holidays to clear up the backlog."

Our concerns are natural! If the UP cannot handle a small merger, how is it going to manage a larger merger? In fact, another suspicious occurrence has arisen. We have learned from various sources that the SP will not be serving Wichita or Winfield, Kansas until the month of January 1996. The newspaper articles inform us that the UP-SP merger application filing date is December 6, 1995. We are concerned, because what type of service will evolve if the UP is to control the SP railroad operating practices? From an unbiased source we have learned that the SP is utilizing the BNSF tracks for container trains and services. How are the small businesses on those lines going to receive service, if the main line continues with additional traffic?

Our members worked diligently and vigorously to obtain the SP competition in the corridor illustrated above. Skill's President spent two days with the SP team showing these fine employees the entire Wichita switching district and he participated in a scheduled meeting with the Wichita Terminal switching railroad concerning the Wichita switching district. The UP-SP merger may be filed on Dec. 1, 1995. When it is filed all of the work the Kansas Shippers Association members performed will be jeopardized. We are back where we started before the BN/SF merger was consummated.

My respect for the SP employees continues in spite of the UP-SP merger. Skill accorded two SP employees the cordial and welcome mat in a recent visit and obtained information for them in order that they would perform well when the SP serves the Wichita area. Their dedication to performance is unsurpassed in railroad history knowing full well when the merger may occur they might be unemployed.

SHORT LINE RAILROAD CUSTOMER CONCERNS

Until recently, a shipper on the CKR railroad needed cars to ship his wheat only to wait for said cars which were not forthcoming from the BNSF railroad. He had no option but to truck wheat to the destination involved in his sales.

Two other shippers, one on the KSW, the other on the main line of the BNSF, cannot ship by rail because their rail rates are prohibitive to the destinations involved in the sales.

This situation is compounded by the further rail concentration created by the subject merger. Without competitive options, the shipper is at the mercy of these mega carriers. Restoration of a competitive balance in south central Kansas is essential to the survival of the rural economy of the region.

The granting of trackage rights by the proposed merger partners UP-SP to the BNSF railroad caused consternation to our members. On movements of grains, they will not compete in sales to Pacific Northwest because of BNSF competition in the Dakotas. The UP-SP will move grains from Nebraska, Colorado and Northwest Kansas to the West Coast not to any degree from SP points in Kansas. By opening up the BNSF to the California, Arizona markets, additional Texas origins will gain an advantage over our members.

Attached is a color coded map of the rail lines in Kansas. Notice how the UP has abandoned older main lines of the MP and concentrated its service on the UP main line in the northern portion of the state. It is using the old MKT line as its present main line running north and south through Wichita and Caldwell, Kansas.

MEGA CARRIERS CONCENTRATE SERVICE

The BNSF has concentrated its efforts to supply service, LO Hoppers and rates at Superior Nebraska, Salina (with the CKR to Abilene) Hutchinson, Wellington and Enid, Oklahoma. The UP has concentrated its service at Salina, Wichita, Hutchinson and Topeka with the same degree of service. The SP has concentrated its service at Hutchinson, Kansas. What is missing in the above service rendered ? **The BNSF at Wichita!**

DEPARTMENT OF JUSTICE SHOULD RECEIVE TRANSFER OF ICC FUNCTIONS ON RAILROAD MEGA-MERGERS

The facts enumerated below under the heading "Ghost Town Appearance of Wichita Grain Elevators " gives impetus for the U.S. Department of Justice to litigate railroad mega carrier mergers. Why are we concerned? It appears that the mega carriers have chosen which areas to serve. This is accomplished by restricting service, preferring shippers with contracts, forcing shippers to truck because of lack of equipment, and controlling short line railroad rates. Reference to the above paragraph is one just one of many examples.

Illustrations of detrimental activity by mega carriers to small businesses are pertinent to this panel meeting. Skill Transportation has knowledge of one of the three mega carriers who has refused to give a railroad contract to a company who has country elevators on its line and a 75 car loading capacity elevator. It has given a contract to other grain interests to move grains from the same Kansas origins to the same Kansas destination.

Skill also has knowledge of said activity in another county of Kansas. A mega-carrier has preferred a certain shipper on its line without giving a grain contract to competing customers adjacent to the preferred customer. The competing customers sought to be treated fairly with their requests. This mega carrier refused to help said customers, thereby causing a disruption of marketing and movement of grains away from these facilities.

GHOST TOWN APPEARANCE OF WICHITA GRAIN ELEVATORS

A visit to Wichita will reveal that there are some 75 car loading facilities standing tall with no activity because they are empty. These are located in the Wichita switching district. Is this the case at these other locations illustrated above? The answer is No! For example, Hutchinson is full of grain and the Wichita elevators, which have some activity, are only storing ten percent of their capacity with wheat.

The exception is Enid where Farmland Industries has ample storage and has closed one of its larger facilities. Small grain elevators businesses, in order to survive, have to go with railroads' policies. Truck grain to certain locations who have grain or product contracts to obtain better FOB elevator prices. Why not Wichita? Geographical location and railroad practices dictate the thrust of marketing. Kansas is the largest wheat growing state in the United States. The farming communities, the farmers, and rural area towns have endured hardships. Core values they have sheltered will be cast aside by mega carriers' policies.

The greatest amount of Kansas hard winter wheat is produced in the counties south and southwest of Wichita. The short line railroads, KSW and CKR, as well as the BNSF and UP serve this area. It is obvious from the facts submitted heretofore, that another carrier is needed, namely, the Kansas City Southern (KCS) Railway to help these small businesses survive.

ICC RESPONSE TO OPEN ACCESS

Another fact which surprised the Kansas Shippers is the ICC response to the Kansas Grain and Feed Association comments concerning the sun setting of the ICC and the proposed UP-SP merger. Our members, as well as KGFA members, support open access to all carriers. As a member of the NITL League, there is knowledge that it supports open access to all carriers. What was the ICC's response?

The ICC'S Chairperson wrote President Tom Tunnel a letter on the KGFA issues, dated October 30, 1995. The following quotation, in part, explains our concern:

"You also discuss the need for open access where more than one rail carrier serves within the switching limits of a given location. In this regard, your members can pursue competitive access relief in individual cases under the Commission's rules at 49 CFR Part 1144."

"I assure you that the Commission is sensitive to the needs of all shippers, both small and large, as well as the needs of the rest of the transportation sector. If I may be of further assistance, please do not hesitate to contact me."

Small businesses do not have the finances to pay the ICC fees for filing a protest, pay attorney or ICC Practitioners fees, as well as afford the time and effort to be away from the business to pursue this important issue. The Department of Justice could deal with it, as the ICC did not, by changing the procedure when handling this issue in a railroad mega-carrier merger case.

THE KCS CONDITIONS

The majority of the Directors of the three shippers associations voted to participate in the merger procedure as noted supra. They also voted to have Skill's President contact the KCS railway seeking information as to whether the KCS would preserve the competitive balance in the region as a replacement for the SP railroad. The KCS would replace the SP rights from Kansas City to Hutchinson via Newton and Wichita to Winfield, Kansas thence over the ATSF line to Dallas-Ft. Worth area. From Dallas-Ft. Worth the UP-SP could give the KCS operating rights to Corpus Christi to hook up with the Tex-Mex Railroad. We support the KCS operating rights as suggested herein.

THE KCS MEETING IN WICHITA

A railroad president has not visited the city of Wichita for at least 15 years. President Michael Haverty's visit will long be remembered in the state of Kansas because on September 28, 1995 at 5:15 a.m., the main water line broke and the city of Wichita and the surrounding communities on the city water service only received a trickle of water. The meeting was well attended regardless of the lack of water. President Haverty gave us insight as to the proposed merger and stated his railroad would help to preserve competition in this corridor.

KCS RAILWAY TO PROVIDE COMPETITION TO ALL SHIPPERS

Why are the small shipper businesses supporting the substitution of the KCS Railway in lieu of the SP? The answer is simple. It may provide the competitive access to this corridor which one of the mega carriers has overlooked! Why the KCS? Its President is a fourth generation railroad Kansan and a former President of the ATSF Railroad. The KCS is a smaller Class I carrier that cares for its shipper customers. Not only will the agriculture interests be involved and competitive, but Kansas intermodal shippers and receivers will benefit from this

railroad service. There are many Kansas small container and TOFC shippers and receivers who must obtain service by the motor carrier mode, to and from Kansas City and/or Tulsa, Oklahoma.

This replacement railroad, the KCS, has generated much interest of the Kansas World Trade Center, and the Wichita Foreign Trade Zone by committing to operate an intermodal facility in Wichita, Kansas provided its railroad will be able to obtain trackage rights in and out of Wichita, Kansas. Has the UP or SP ever made that type commitment? Has the BNSF in the past ever made that kind of commitment?

CONCLUSION

This meeting held on November 8, 1995, and the testimony rendered and heard thereat may provide a base for help to all small businesses in the USA in this mega carrier atmosphere. This statement and the other statement received at the November, 1995 meeting reveals that many shippers are doubting the input data being provided by the mega carriers. We are attaching copies of the statement of Larry Coffman, who is a member of the Kansas Shippers Association, which adds to the others rendered at the meeting of treatment to small business by mega carriers

PRAYER FOR HELP

There is a need of the Department of Justice to litigate future mega carrier mergers. Small Kansas grain businesses and farming communities pray that the November 8 meeting will give impetus to receive help from their elected representatives and the federal agencies. In addition, the substitution of the KCS Railway, the added third carrier at Wichita, will provide the competition necessary to help the other shippers who have need of an intermodal facility in Wichita. The KCS Railway's posture to obtain the SP's trackage rights and your active consideration of this issue will prevent both a small grain elevator and possible others from being added to the Ghost Town Appearance. It is the only fair solution that small businesses exist in today's transportation atmosphere when two railroad mega carriers are attempting to "carve up" all the territory west of the Mississippi River.

I, James J. Irlandi, declare under penalty of perjury that the foregoing is true and correct. Further, I certify that I am qualified and authorized to file this verified statement. Executed on November 13, 1995.

Respectfully submitted,

Jim Irlandi

James J. Irlandi
President

APPENDIX A-1

QUALIFICATIONS OF JAMES J. IRLANDI

Education

A. General.
   1. Graduated from Bulkeley High School New London, Connecticut.
   2. Attended Connecticut State University for 2 years.
   3. Attended night school at the University of Wisconsin for 10 years and a seminar at Marquette University.
   4. Certificate of Transportation Traffic Management from the University of Wisconsin.

B. Marquette University Seminar General Business.

C. LaSalle Extension University.
   1. Graduated with a BS degree in law.
   2. Took 4 years of law training for business leadership.
   3. Graduated from the traffic course (2 years).
   4. Was elected to membership of the Traffic and Transportation Advisory Council.

D. Graduated from the ICC law course at the University of Wisconsin and passed all federal exams -- ICC-FMB.

E. Passed all exams -- Certificate of American Society of Transportation & Logistics (Similar to CPA exam).

F. Distribution and Planning Specialists -- seminars.
   1. Railroad costing and analysis.
   2. Motor carrier costing and analysis.
   3. Advanced railroad costing and analysis.
   4. Waterways costing and analysis.

Employment

A. 40 months with the U.S. Army.

B. Worked 2 years at the NYNH&H Railroad.

C. Worked 16 plus years at Krause Milling Company in Milwaukee as the Director of Transportation -- export, import, domestic rail, truck, and barge.

D. Was with Garvey and SRI, Inc. at Wichita for 23 years as Vice President of Transportation; all phases of transportation.

E. Private consultant for 10 years.

Recognition

A. ICC and Association for Transportation Law Logistics and Policy recognizes James J. Irlandi "For Services to the Transportation Profession and to the Commission and Its Bar Association for More Than Forty Years." Presented June 1995.

B. Listed in Who's Who in the Mid-West, 1976-77 edition.

C. Listed in Leading Men in American Transportation, 1967 edition.

D. Founder Member, Wisconsin Chapter ICC Practitioners.

APPENDIX A-2

SHORT LINE AND MAINLINE SHIPPERS HAVE INTERLOCKING RAILROAD SERVICES

Shipper concerns are also related to ownership of facilities on more than one railroad.

I. Short line and Mainline Shippers.
   - A. SSW, CKR - Mainline BNSF Shippers.
     Some SSW shippers are also located on the mainline of the BNSF - Hutchinson - west; others are on the Herington to Liberal SSW mainline.
   - B. KSW - CKR and mainline BNSF shippers.
     Three shippers are on the mainline of the BNSF - Wellington - west; they have facilities on the KSW and CKR short lines.
   - C. DCF&B - BNSF.
     Two shippers who have facilities on the Hutchinson - west mainline have facilities on the Dodge City - Ford & Bucklin Railroad.
   - D. CKR - MOPAC.
     One shipper has three facilities on the CKR and two on the MOPAC - Pueblo mainline.

II. Short Line Shippers.
   - A. SEK - SKO.
     One shipper located at Humboldt, Kansas, on the SEK, ships cement, grain and other commodities.
   - B. KSW Railroad.
     Two shippers are located on the KSW.
   - C. CKR Railroad.
     One shipper has five facilities on the CKR; others have one or more.

III. Mainline Shippers.
   - A. Former RI now MP Railroad.
     One shipper is located on the MP, which was a former RI and OKT station.
   - B. Former BN now BNSF.
     One shipper was switched by the BN, and now will be on the BNSF --open to the UP-SP.
   - C. KSW -UP.
     One shipper who is switched by the KSW is considered on the mainline of the UP.
   - D. SSW - BNSF - Future UP - SP.
     One shipper with two facilities at one station was switched by the SSW and ATSF and is now open to UP. We will have only two carriers in the future: the UP-SP and BNSF. In my opinion, this shipper needs the KCS Railroad for additional competition.

BEFORE THE SMALL BUSINESS COMMITTEES
OF THE U.S. HOUSE OF REPRESENTATIVES
AND THE U.S. SENATE
RAYBURN HOUSE OFFICE BUILDING
NOVEMBER 8, 1995

RE: UP-SP Merger- ICC Finance Docket No. 32760

My name is Larry H. Coffman, grain department manager of Farmers Co-op Association, Lawrence, Kansas. We have 16 grain elevators on several railroads located in northeastern Kansas. We are a receiver of grain from farmers and therefore a shipper. We ship both by rail and truck to several different markets. These being both interior and gulf shipments.

I have had experience of railroads merging and the results that follow. When the UP-MP merger took place our facility at Overbrook, Kansas service was discontinued because of small wash-out. The line was abandoned north and so we became a branch line. The MP illegally closed our branch line while it had the line embargoed. We appealed to the ICC and won our case in that tribunal. After nearly 10 years of litigation, without any help from our grain industry, we settled the case. It is now known throughout the agricultural industry as the "Overbrook Case"

We are experiencing the BN-ATSF merger now with our rates from some locations almost double what they were last year. As time goes on we are finding it is almost impossible to negotiate any thing for the 25 car loading capacity that we have at one of our locations that we have used for the last 15 years.

It is very apparent to us that the larger the railroad gets the farther away from the shipper out in the country. Our contacts with railroads after these mergers become fewer and fewer. It is very clear that they have an agenda of the business that they want and they are not interested in the other business.

Respectfully Yours

Larry Coffman

Larry H. Coffman
Grain Dept Manager

overlapping areas. Nevertheless, the evidence submitted by the parties identifies a number of specific traffic corridors and areas of parallel competition where the merger would eliminate intramodal competition by reducing the number of serving railroads from 2 to 1. These areas are: (a) the corridor traversing Amarillo and Lubbock, Texas between Pueblo, Colorado and Fort Worth, Texas; (b) the Fort Madison/Keokuk, Iowa to Galesburg, Illinois area; (c) the area around Wichita, Kansas; and (d) service to Superior, Nebraska

DOT believes that the voluntary trackage rights and haulage agreements the Applicants have negotiated with the UP, SP, KCS, and several short line railroads will effectively mitigate the loss of parallel competition that would result from the merger. [11] DOJ generally agrees with this conclusion, subject to the prescription of cost-based trackage rights fees by the ICC to ensure competitive rates and service after the merger. DOJ-3 at 11. [12] Without endorsing the specific terms of these agreements, DOT urges the ICC to impose as a condition on the merger only those portions of the voluntary

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11/ Indeed, collectively the agreements act to increase rail competition above the level that now exists because they grant access to third-party rail carriers in areas unaffected by the proposed consolidation. SP's overhead trackage rights provide access to industries and connecting carriers at the origin and destination points and to industries and shortlines at intermediate points such as Kansas City and Wichita, Kansas, at Amarillo, Lubbock, and Plainview, Texas, and at Fort Madison, Iowa and Galesburg, Illinois. UP's rights between Superior, Nebraska and Abilene, Kansas not only resolve the competitive problem at Superior, but enable UP through its connection at Abilene to provide a more direct route for grain moving to export points at the Gulf. The haulage rights granted KCS to Omaha/Council Bluffs provides the area with an additional competitor, and the combination of haulage to the Southeast, access to Houston port terminal railroads, access to industries in Fort Worth, and authority to market coal from the Powder River Basin (including rate making) on behalf of the Applicants introduces new competition into these areas, and strengthens KCS's competitive position.

12/ DOJ continues to be concerned about reductions in competition at Borger, Texas, and at Oklahoma Gas and Electric's Red Rock plant. Both locations involve special issues of parallel competition with "uncommitted" market participants. DOT addresses these issues later in this brief, and in the Confidential Appendix hereto.

agreements that are necessary to resolve the competitive problems noted above. [13]

1. Other competitive conditions

Several parties have requested additional trackage rights as a condition of the merger. The Department considers such conditions unwarranted.

(a.) KEOKUK JUNCTION RAILWAY ("KJ")

The KJ presently competes with BN for traffic moving between Keokuk and Fort Madison, Iowa, where its traffic is interchanged with Santa Fe. KJ moves its Keokuk traffic east to La Harpe, Illinois, to a connection with the Toledo, Peoria and Western Railroad ("TPW"); the TPW then hauls the traffic west again to interchange with Santa Fe at Fort Madison. To resolve the reduction in competition that would occur between Keokuk and Fort Madison as a result of the merger, Applicants have offered KJ a connection with SP at Bushnell, Illinois, reached via the TPW from La Harpe

Because Bushnell is several miles east of La Harpe, KJ believes it would be an unsatisfactory connection for westbound traffic. It has requested unrestricted trackage rights south over BN's line between Keokuk and West Quincy, Missouri, to connect with SP, and overhead rights from West Quincy to Hannibal, Missouri, to reach the Norfolk Southern Railroad. KJ also requests access to industries along the BN line to West Quincy, and other concessions.

The Commission should deny these requests. The additional miles eastward required to reach a connection with SP at Bushnell are not sufficient to affect the long haul movements to/from the West that KJ handles. E.g., the difference in distance between Bushnell versus La Harpe/Fort Madison to Los Angeles is 47 miles. BN/SF-

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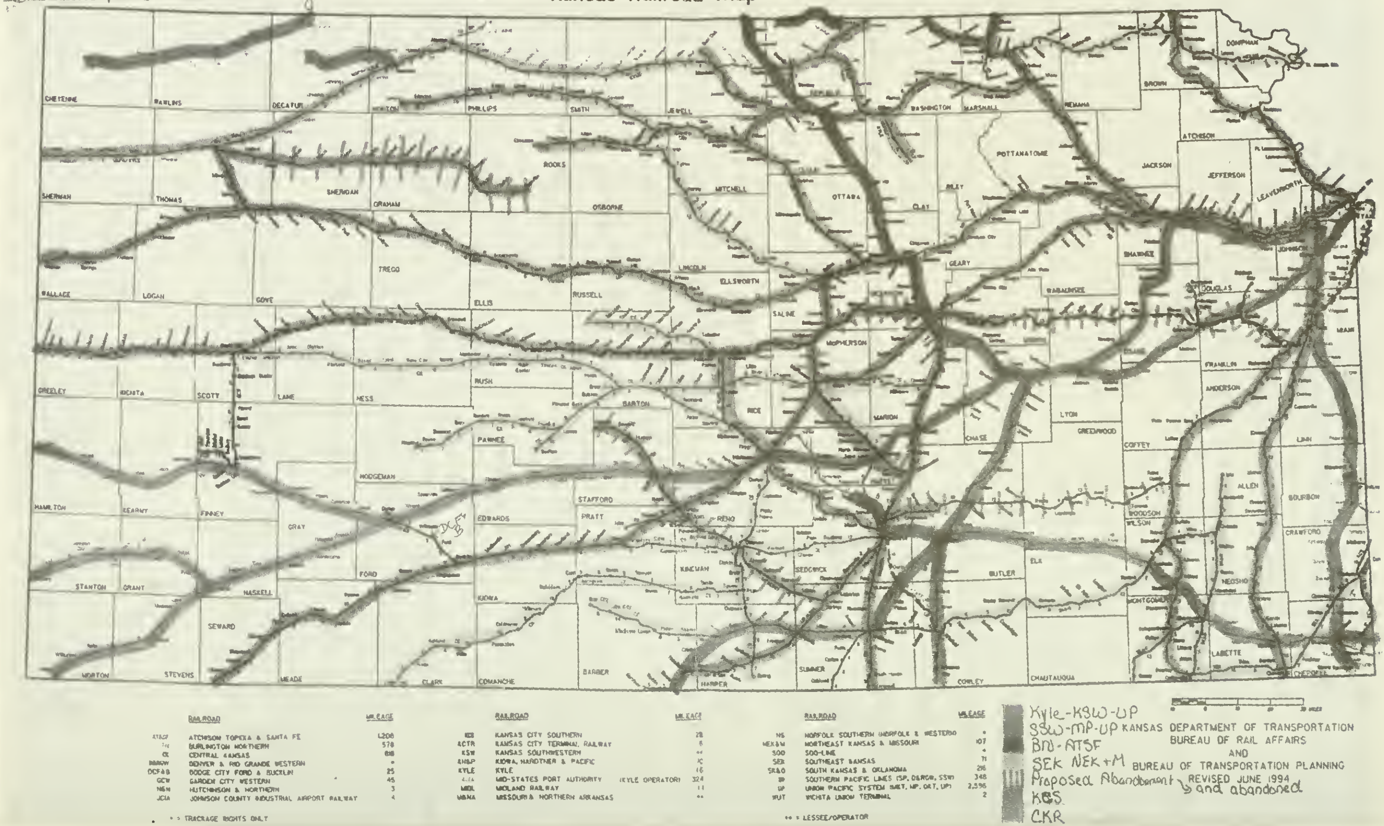
13/ The inclusion in a condition of the rights granted in the Stipulation entered into with NITL may be more extensive than is necessary to address these harms.

Transportation Consulting Inc.

Kansas Railroad Map



REPORT TO

JOINT COMMITTEE OF THE HONORABLE

U.S. SENATE & HOUSE OF REPRESENTATIVES

COMMITTEES ON SMALL BUSINESS

IN THE MATTER OF:

RAILROAD CONSOLIDATION AND SMALL BUSINESS

NOVEMBER 17, 1995

FOLLOWING MEETING OF

NOVEMBER 8, 1995

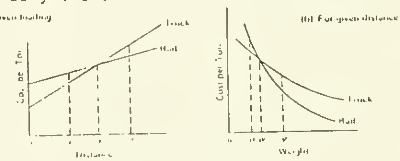
BY

ARTHUR KUNGLE JR
BOX 365
ANNAPOLIS, MARYLAND 21404
CITIZEN

Federal interest in transportation in the early 19th century promoted roads and canals in the new midwest and just before our civil war first aided start-up of the Illinois Central (8), and then some of the many routes proposed for Pacific Railways (36)--which began a vast building race to the coast, treasured in American and Canadian history (12, 19: pg. 2). This led to adventures and amalgamations, which eventually grew to threaten farmers and small businessmen and led to the formation of the Interstate Commerce Commission (12). Necessity for national transport unity and efficiency in WWI brought nationally run systems in both Britain and America (26, 12). Usual belief is that truck and air competition with rails sprang up over night from building of new highways, but it was the war time investment in human capital by our nations that taught farm and city lads how to drive, fly and care for internal combustion machines (26, 19), and pompous railroads and regulations sacrificed high ticket items for low rate bulk haulage (26, 19)*.

In 1929, U.S. leadership pushed the ICC to a grand plan for railroad consolidation in the US & Canada into 21 systems--mostly wedding weak to strong--but opposition in Congress and finance allowed only gradual changes as possible (11, 20, 14, 15, 7). The depression, rail bankruptcies, and migration of people, enterprises and political preferences deferred further action until after WWII (12). Then post-war economic revival brought new interest in transport economics and competition (16, 26). Masters of economics, Schumpeter and Stigler warned about loose talk about competition (27, 31). In transportation, perfect competition is an ideal, but local monopoly and larger oligopoly are norms and over regulation a familiar impediment (8, 13, 29).

*13: 247: Dr Kneafsey shows Truck - Rail Cost Relations:



Grain car shortages were predicted, following the rise of special function rail cars and the decline of general box cars (13: 297, 1, 2, 3), similar problems faced Canada (19), with whom we share continental laboratories of liberty, and from whom we learn deregulation lessons (24).

Some argue good enough competition only comes with many competitors (8, 29)*, and others say that oligopolies can fairly and fiercely fight for business (25, 32), while still others claim that functioning in space and time considerations offers broader dimensions and sounder understanding than older linear economics (9, 12).

* The local, Annapolis, Public Library supplied E. Schwaertz's--clear and simple-- Econ 101½, which shows that "competition comes in many packages", each with different characteristics, with credit to her:

Perfect ompetition:
- firms are small --many buyers and seller--market enty and exits..relatively inespensive--firms are price takers: supply and demand shape..charges-- difficult to distinguish producers of same item.

Monopolistic competition:
- firms (usu.) not very large--competitors..number--twenty to eighty--market entry & exit relatively easy--firms are "price takers" charging (about the same as) others similar--(every effort made) to distinguish products..and convey their unizue qualities.

Oligopolies:
- firms are large, (usually) only three to twelve firms (do) more than half a market's (business)--market entry and exit, expensive (and hence) difficult-- firms are "prime makers" (also 19:10)..pricing usually relates more closely to production costs and profit goals than to competitive consideration--customer attraction (usually) (by product differentiation) and non price (considerations).

Monopolies:
- firms tend to be very large--with one seller dominant--market entry and exit are difficult because of--the power and size of the dominant firm (and also often times because of the market involved)--firm has the power (to shape levels of price and production--the invisible hand appears when consumers respond to low prices and buy more or to high prices and buy less.

(How excellent the lady is in her descriptions!)

At the hearing of the joint committee, concerns were raise about rail combinations, competition, service and labor--the latter, though of ancestors mine, said the same as the Gov. of New York in 1829 complaining to the President about the coming of railways and its threat to canal workers, shipbuiliders, and passengers "propelled at the insane speed of 15 miles per hour...God surely never meant people to travel at such hellish speed."(19:16-17, thanks to our northern neighbors for this jewel.) Witnesses differed about western mergers and their merits. American railroads are moving toward two great western systems (BNSF and UP dividing up SP), and three great eastern systmes (CSX, NS and Conrail--where, again, the stronger will surely divide up differences between them), but note well, Sp's 1% rail tie replacement rate augurs well for future disaster (1, 2, 3). This east - west bias (34: esp. anchoring under conditions of uncertainty) neglects both mid-American, and running north and south, KCS & IC, and also Canadian and Mexican neighbors with similar, parallel and related interests (19, 17). (The saga of today's rail struggles play out on the daily transport press (30, 21, 33, 17). ICC transformation into TAP may move regulators to consider greater interests than mere effieciency in transport matters (35), but true consideration of our nation's railroad and infrastructur future must be founded on where the rails run. Rand McNally's trusty 1948, and Drury's excellent historical and modern, railroad maps are sure guides to acompany the splendid map resources of the Library of Congress and ICC library--now in danger (5, 6, 23, 22, 36).

The solution of rails transport problems may become simple. Let CSX & NS be considered as cross x's (NE-SW, SE-NW), using coast & mountains, and let upright cross Xs be used for all eastern lines above the Ohio river (just add Conrail). All western lines run to the Pacific, first UP (&CP=Central Pacific) center, then BN northern, and SF and SP southern, routes (noting DGRW followed UP).

-4-

IC & KCS parallel the Mississippi and the would-be Midland Continental (22) routes, similar to the first land grant canals (Wabash R. to L.Erie and Illinois R. to L. Michigan (7)). IC & KCS should team up with CN's Grand Trunk and CP's Soo, and thus in mutual strength reaching north and south, providing better markets and competition for three nations and people in growing alliance. This prospect may not please behemoths east or west, for without such unity midcontinental lines will be beaten to pieces and those pieces picked up and divided among eastern cross X's and western pacific run--and mid- America, Canada and Mexico will prove the loser. Our continent's peoples will be better served, even if with fewer rail service firms, with strong mid-North American rail, truck and water service and competition.

May the Good Lord grant that this be true.

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34. Tversky, Amos, & Daniel Kahneman, "Judgement under uncertainty: Heuristics & Biases" (=book title, Kahneman, ed.), Cambridge, 1982

35. U.S. House of Representatives, Committee on Transporatation and Infrastructure, ICC Termination Act of 1995, Report, Nov. 6, 1995

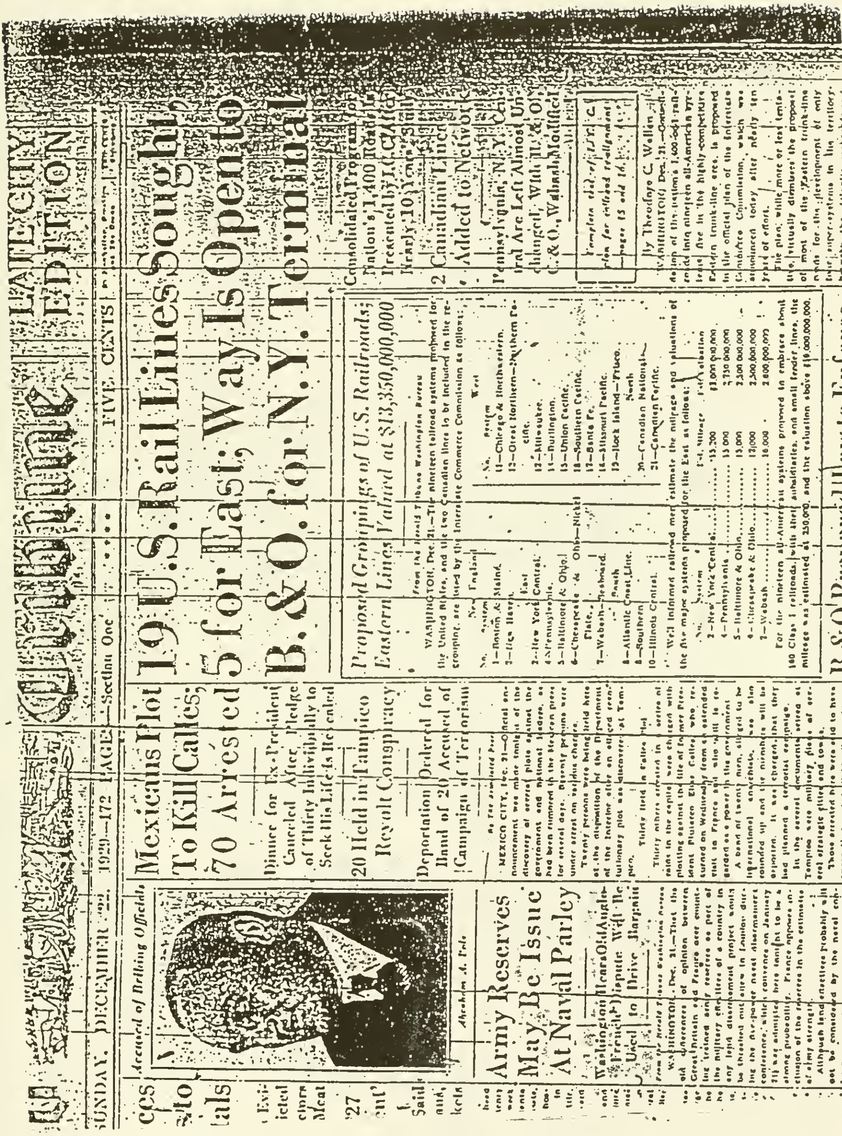
36. Warren, G. Kemble, map of routes for a PACIFIC RAILROAD, compiled to accompany report of Hon. Jefferson Davis, Sec. of War, 1855, Library of Congress, Map Div. (=pg. 34-35 of Modeslski above, who reports this is Millard Fillmore's copy).

APPENDICIES

Numbers above: 36 (from text, copy of original not readily reducible),

20 and 23.


MAP OF ROUTES
PACIFIC RAILROAD



Tribune — LATE CITY EDITION

SUNDAY, DECEMBER 22, 1929—172 PAGES—Section One — FIVE CENTS

19 U.S. Rail Lines Sought, 5 for East; Way Is Open to B. & O. for N.Y. Terminal

Proposed Groupings of U.S. Railroads; Eastern Lines Valued at $13,350,000,000

From the Herald Tribune Washington Bureau

WASHINGTON, Dec. 21.—The nineteen railroad systems proposed for the United States, and the two Canadian lines to be included in the re-grouping, are listed by the Interstate Commerce Commission as follows:

New England	West
No. System	No. System
1—Boston & Maine.	11—Chicago & Northwestern.
3—New Haven.	12—Great Northern—Northern Pacific.
East	12—Milwaukee.
2—New York Central.	14—Burlington.
4—Pennsylvania.	15—Union Pacific.
5—Baltimore & Ohio.	16—Southern Pacific.
6—Chesapeake & Ohio—Nickel Plate.	17—Santa Fe.
7—Wabash—Seaboard.	18—Missouri Pacific.
South	19—Rock Island—Frisco.
8—Atlantic Coast Line.	North
9—Southern.	20—Canadian National.
10—Illinois Central.	21—Canadian Pacific.

Well informed railroad men estimate the mileage and valuations of the five major systems proposed for the East as follows:

No.	System	Est. Mileage	Est. Valuation
2	New York Central	15,300	$3,000,000,000
4	Pennsylvania	15,000	3,750,000,000
5	Baltimore & Ohio	15,000	2,500,000,000
6	Chesapeake & Ohio	12,000	2,500,000,000
7	Wabash	16,000	2,600,000,000

For the nineteen all-American systems proposed to embrace about 160 Class 1 railroads, with their subsidiaries, and small feeder lines, the mileage was estimated at 250,000, and the valuation above $10,000,000,000.

B.&O. Prepared Law to Enforce

Consolidated Program for Nation's 1,400 Roads Is Presented by I.C.C. After Nearly 10 Years' Study

2 Canadian Lines Added to Network

Pennsylvania, N.Y. Central Are Left Almost Unchanged; With B.&O., C.&O., Wabash Modified

Complete text of I.C.C. plan for railroad realignment—pages 15 and 16

By Theodore C. Wallen

WASHINGTON, Dec. 21.—Consolidation of the nation's 1,400-odd railroads into nineteen all-American systems, five in the highly-competitive Eastern trunk-line area, is proposed in the official plan of the Interstate Commerce Commission, which was announced today after nearly ten years of effort.

The plan, while more or less tentative, virtually dismisses the proposal of most of the Eastern trunk-line roads for the development of only four super-systems in the territory between the Atlantic seaboard and

Accused of Bribing Officials

Abraham A. Fole

Army Reserves May Be Issue At Naval Parley

Washington Hears Old Anglo-French Dispute Will Be Used to Drive Bargain

From the Herald Tribune Washington Bureau

WASHINGTON, Dec. 21.—That the old differences of opinion between Great Britain and France over counting trained army reserves as part of the military effectives of a country in any land disarmament project would be threshed out anew in London during the five-power naval disarmament conference, which convenes on January 21, was admitted here tonight to be a strong probability. France opposes inclusion of the reserves in the estimates of army strength.

Although land effectives probably will not be considered by the naval conference proper, with the possible exception of airplanes operating from land bases, it was believed to be inevitable that ...

Mexicans Plot To Kill Calles; 70 Arrested

Dinner for Ex-President Canceled After Pledge of Thirty Individually to Seek His Life Is Revealed

20 Held in Tampico Revolt Conspiracy

Deportation Ordered for Band of 20 Accused of Campaign of Terrorism

By The Associated Press

MEXICO CITY, Dec. 21.—Official announcement was made tonight of the discovery of several plots against the government and national leaders, as had been rumored in the Mexican press for several days. Seventy persons were under arrest on various charges.

Twenty persons were being held here at the disposition of the Department of the Interior after an alleged revolutionary plot was discovered at Tampico.

Thirty Held in Calles Plot

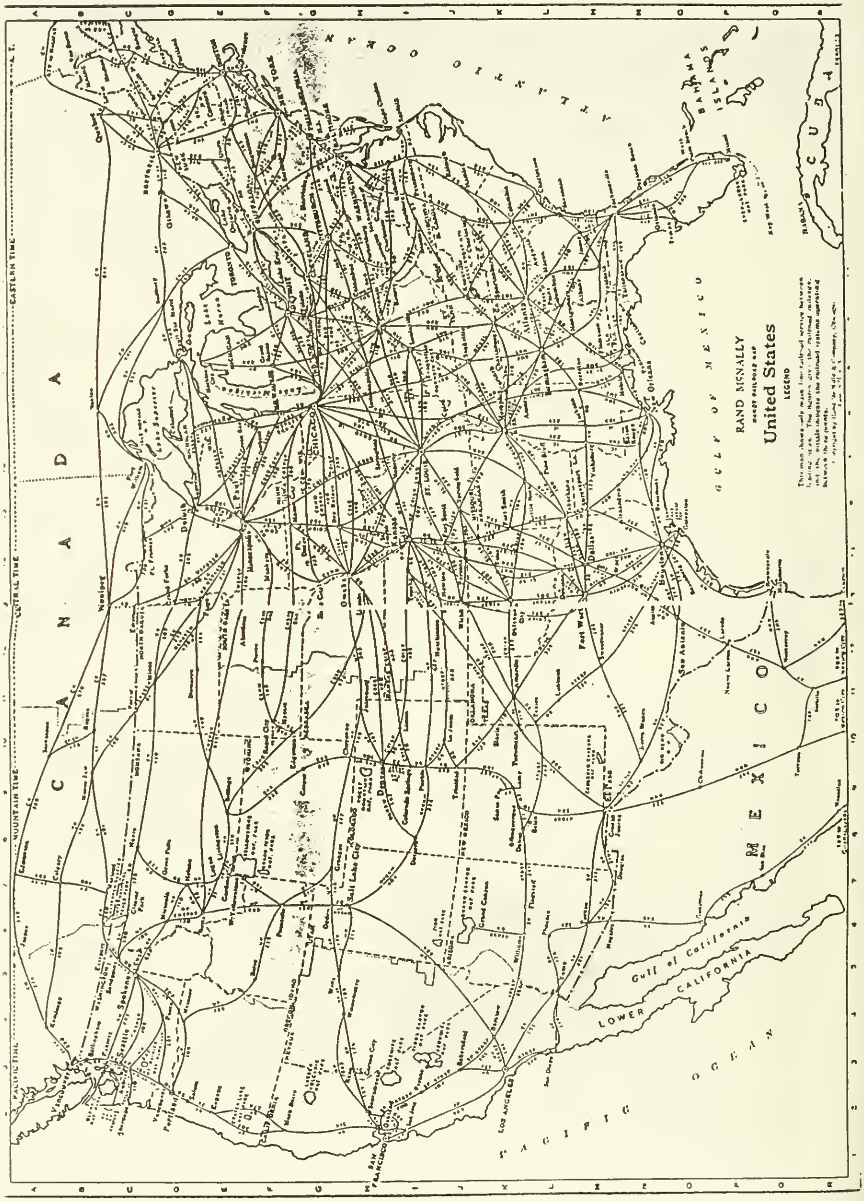
Thirty others arrested in a series of raids in the capital were charged with plotting against the life of former President Plutarco Elias Calles, who returned on Wednesday from an extended visit to France and who still is regarded as a power in the government.

A band of twenty men, alleged to be international anarchists, was also rounded up and the members will be deported. It was charged that they had planned a terrorist campaign.

In the several documents seized at Tampico were military plans of several strategic cities and towns.

Those arrested here were said to have sworn that each individually would attempt to assassinate General Calles.

Plans for a dinner of 3,000 covers ...


RAND McNALLY
United States
LEGEND
CANADA
MEXICO
GULF OF MEXICO
ATLANTIC OCEAN
PACIFIC OCEAN
Gulf of California
LOWER CALIFORNIA
BAHAMA ISLANDS
CUBA
CHICAGO
ST. LOUIS
NEW YORK
SAN FRANCISCO
LOS ANGELES
Salt Lake City
Denver
Dallas
Fort Worth
Houston
Atlanta
Spokane
Seattle
Winnipeg
Duluth
St. Paul
Omaha
EASTERN TIME
CENTRAL TIME
MOUNTAIN TIME
PACIFIC TIME

November 18, 1995

Kind and Gracious Staff
Committee on Small Business
U.S. House of Representatives
2361 Rayburn House Office Building
Washinton, D.C.
Fax 202-225-3587

Gentlefolk,

Herewith are slight corrections in references*in my submission yesterday--which might have been able to be made yesterday, if the Library of Congress had been open:
pg. 1, last line: 8, 13, 24 for 8, 13, 20
pg. 2, last line: 9, 10 for 10, 11 (Greenhut, pater, not Hoover, Pres.)
(and obviously hellish is spelled with an h,
eastern is spelled with an a,
man is spelled with a m, & not a n)
reference #19 is dated 1993, and not 1992--which Dr Grim cited too--
reference #29 is dated 1991, and not 1988.

If it is at all possible, please make these small corrections, for those same will be made on those copies of the report to you that I send out to governors, premiers, FRB presidents and the free press in America, Canada and Mexico.

Thanks for your help in this matter, and when LoC is back open --and my Salvation Army bell ringing is completed--I will try to get some good map copies for you and the transport committees.

May the Good Lord bless you and your families this holy season.

Truly,
Arthur Kungle Jr
Box 365
Annapolis, Md 21404-0365

* Spelling typos are less critical here than numerical tie-ins.
& Finding reading glasses helps, too.

PS This would have gone out [illegible] but then busy days working with relatives & now entertain the 30 years younger guys in my house say this is my problem so I walked in a light drew from [illegible] + Spa to Kudo at Forest Rose ([illegible]) & [illegible] [illegible] provide of this seems [illegible] — my mother save her life for her county caught between governments + peoples (Rot U.S. Rep Gene Taylor [illegible] says check it out with him) — + as the youth should have learned when I left — It is better to sacrifice for God or country than revel in creature comforts. [illegible] God Bless America
Arthur K[illegible]

[illegible] [illegible]

P.P.S. Check weather cut back [illegible] on contributions

November 16, 1995

Petition to the U.S. Congress

Re: Loss and destruction of the ICC library
during ICC Termination and transfer of functions to U.S.Transportation Dept.

Gentlefolk:

With the closing of the ICC and transfer of functions, neither Congressional reports nor libary staff indicate the fate of the books, records and maps in the ICC library. Staff there noted no interest in the collection's fate by the Library of Congress, but report some interest by the University of Denver, and I suggest expertise or interest by theJohn W. Barriger III National Railroad Library, part of the St. Louis Mercantile Library Association. The ICC library is but one of several special federal libraries in our nation's capital--including also excellent FRB, SEC & U.S. Treasury libraries--and it seems in the better interest of our nation and people such historic collections be preserved, for I have found jewels in each, not available in others, and there are surely other treasures in books that other citizens and all our people and nation may yet dearly need in ages yet to come.

Therefore, I ask that the leadership immediately appoint--if there is not already a bi-partisan--committee to safeguard the ICC library, and I further suggest that the Honorable U.S. Rep. Major Owens be entrusted for major judgement in this matter--for he is the only member of Congress nobly in a librarian tradition.

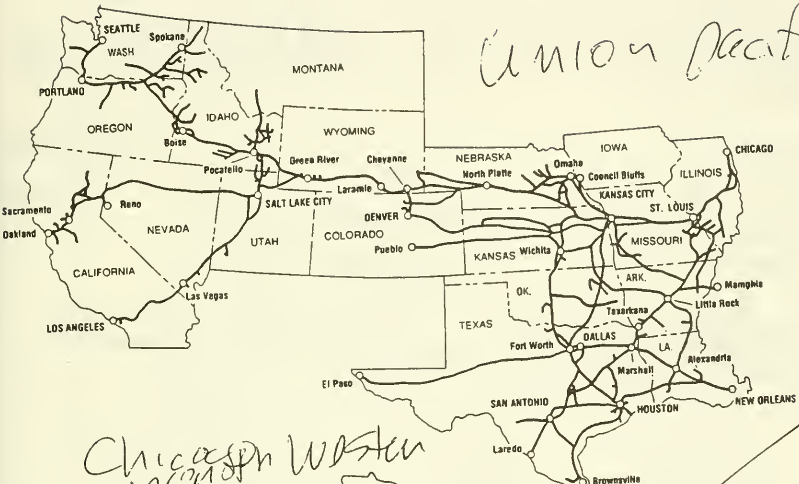
Truly,

Arthur Kungle Jr

copies:
American Libary Association
Barriger National Railroad Library
ICC
Librarian of Congress
U.S. Secretary of Transportation
University of Denver

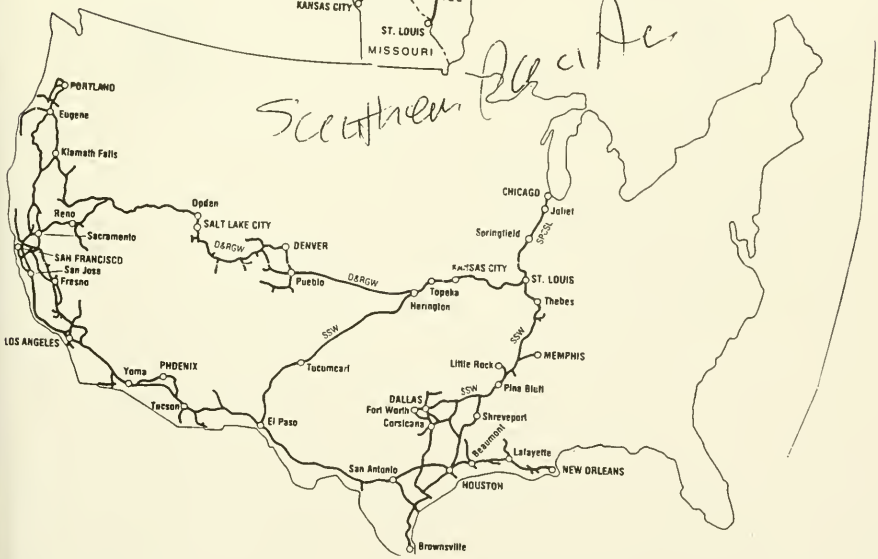
Pacific Lines

Union Pacific



Chicago North Western

Southern Pacific



November 6, 1995

U. S. Congress
House & Senate Small Business Committees
meeting in joint session
Longworth Building
Washington, D.C.

Genthlefolk:

Herewith are railroad maps: marvellous

a. for each house: Railroad Age's 1930 ICC (Congress directed) Railroad Consolidation maps (possibly "lost" until yesterday afternoon); 2 for each comm

b. Rand MCNally's 1948 conitinetntal railroad map;

c. main lines involved today in combinations from George Drury's excellent The Trainwatcher's Guide to North American Railroads and The Historical Guide to North American Railroads (about 1990, from Kalmbach 1-800-533-6664).

d. and if possible railroad routes in 1995. [illegible] off [illegible]

With thanks to Annapolis Post Box, the ICC Library and the good old Library of congress.

2 for each Committee

Truly,

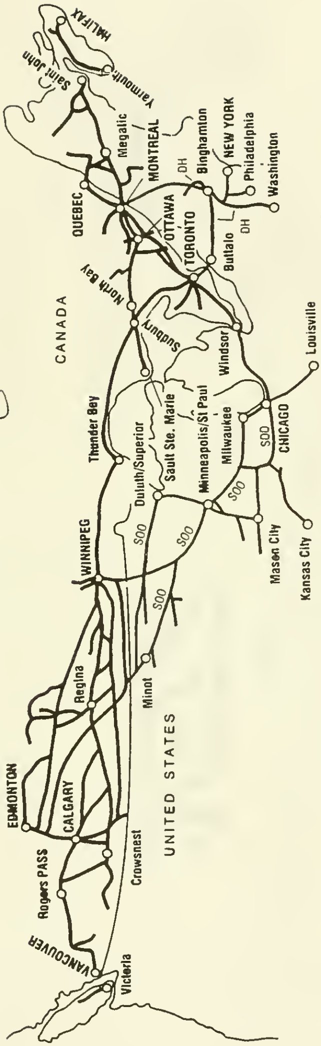
Arthur Kungle Jr
Box 365
Annapolis, Md 21404-0365
(410-263-7330)

+ Excellent copy of 1995 Traffic World — map pg 10 showing Pacific lines — sweetheart deal — with SP Northern to buy off USSD & opposition.

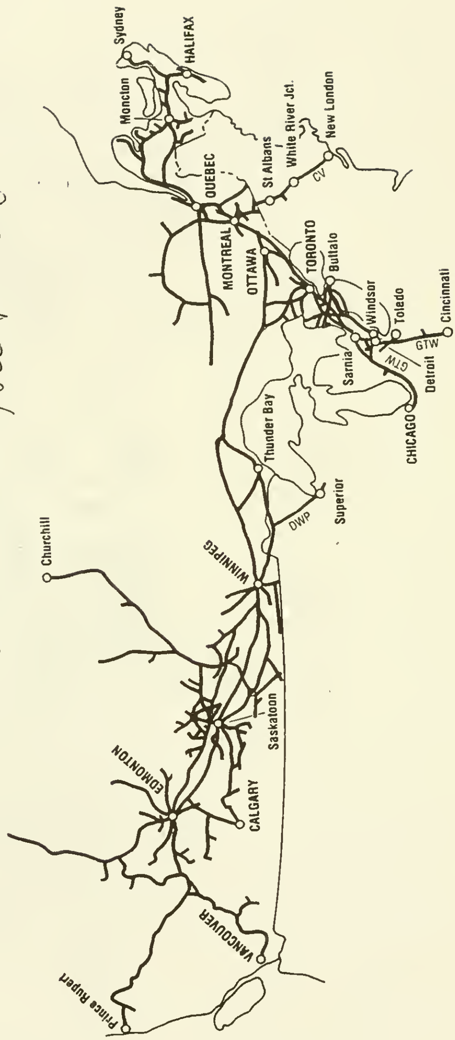
~~160A~~

161B

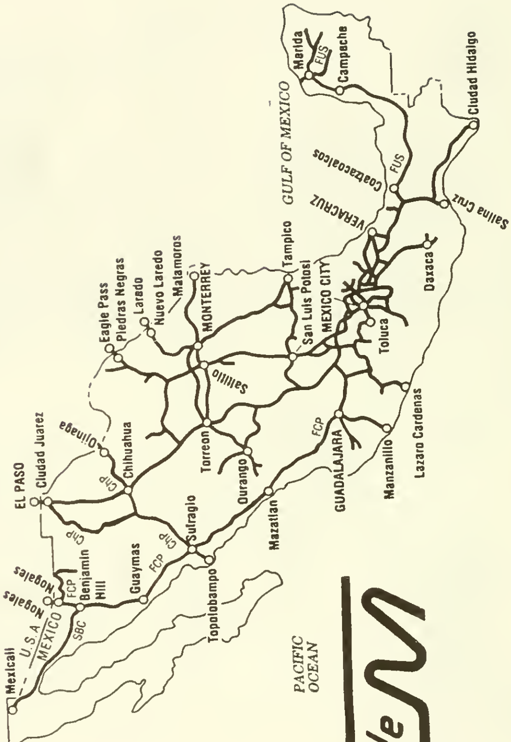
Canadian Pacific



Canadian National

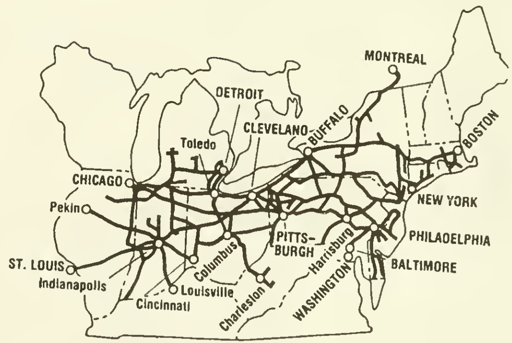


Mexican Railway

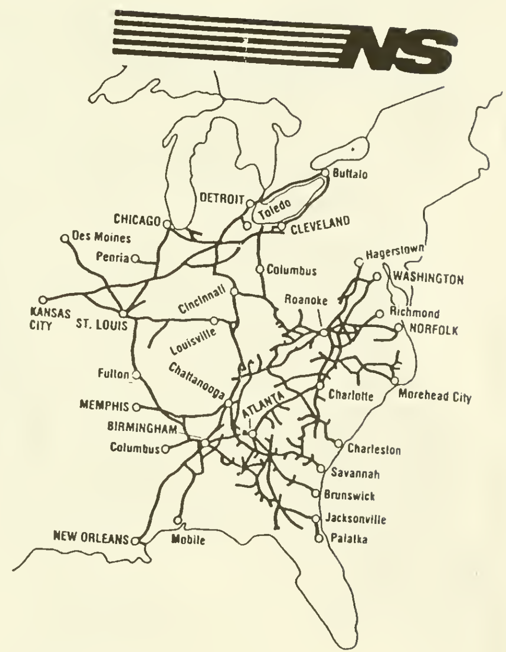


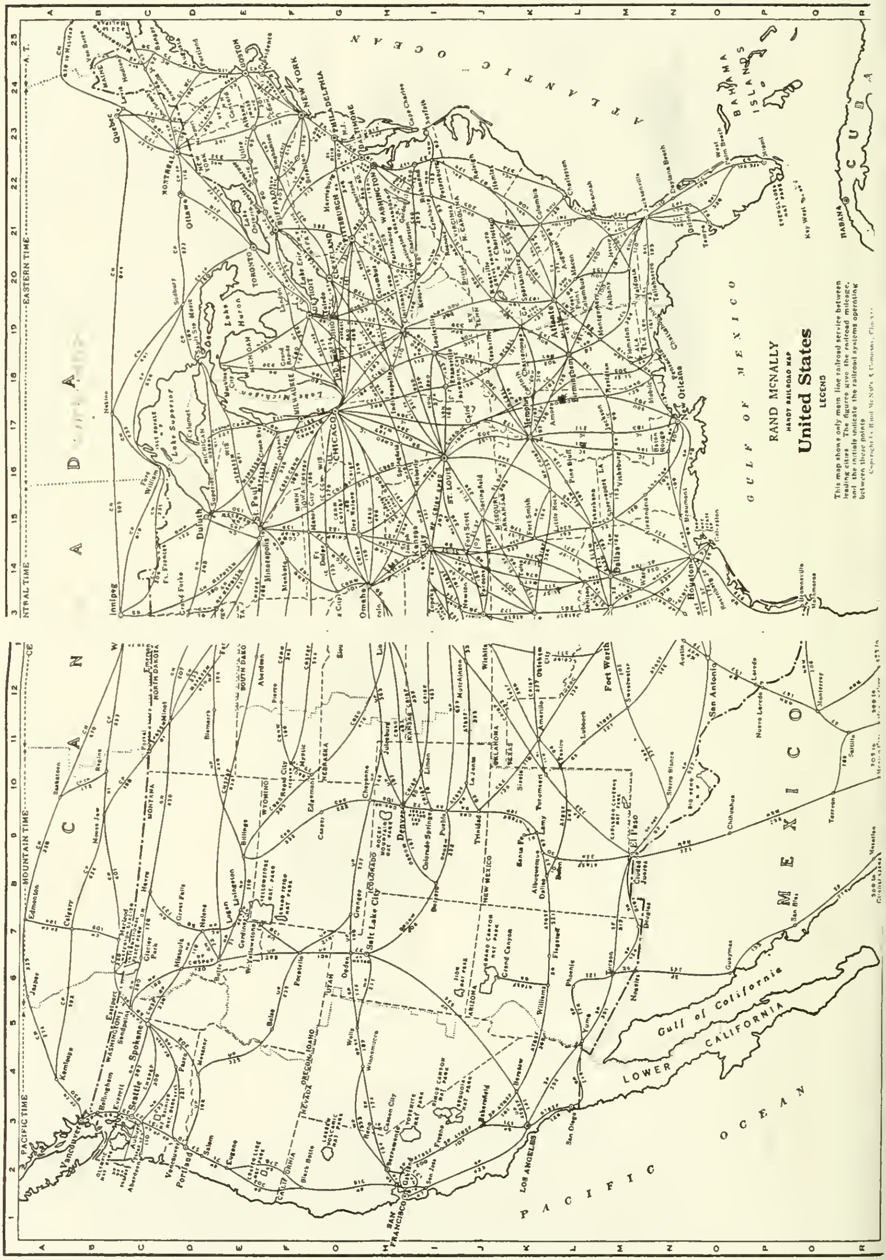
CSX

Conrail

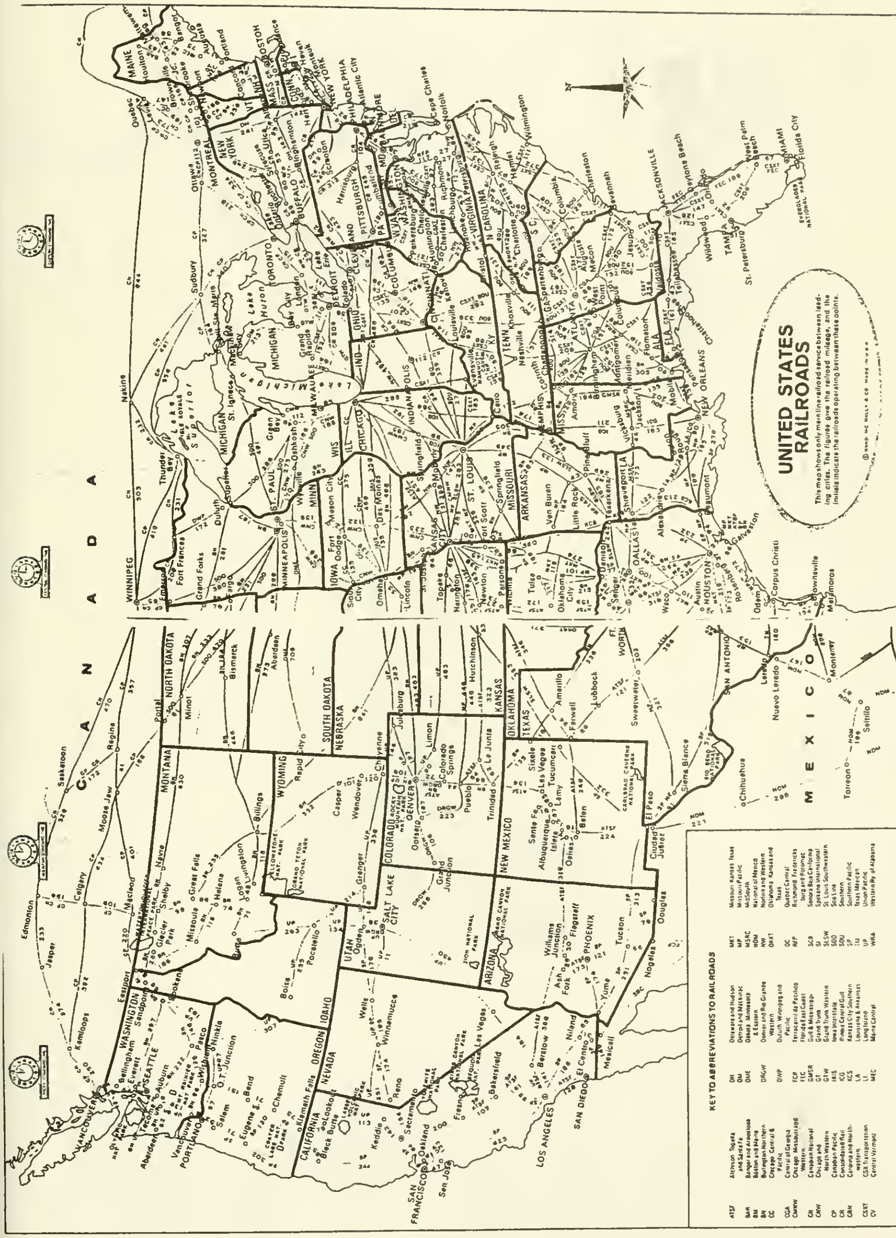


Norfolk Southern




RAND McNALLY
HANDY RAILROAD MAP
United States
LEGEND
This map shows only main line railroad service between leading cities. The figures give the railroad mileage, and the initials indicate the railroad systems operating between these points.
GULF OF MEXICO
ATLANTIC OCEAN
PACIFIC OCEAN
CANADA
MEXICO
Gulf of California
LOWER CALIFORNIA
BAHAMA ISLANDS
CUBA
PACIFIC TIME
MOUNTAIN TIME
EASTERN TIME

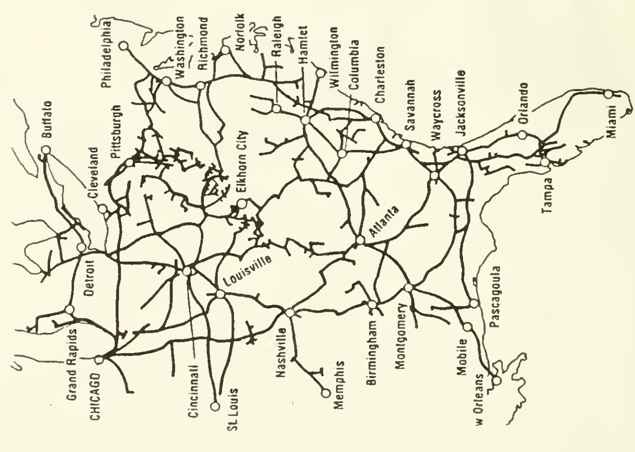
St 91 9

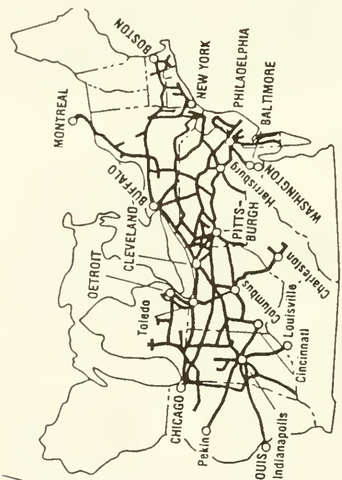

UNITED STATES RAILROADS
This map shows only mainline railroad service between leading cities. The figures give the railroad mileage, and the initials indicate the railroads operating between these points.
KEY TO ABBREVIATIONS TO RAILROADS

CSX Eastern lines

Conrail

Norfolk Southern





Illinois Central

Trans Mexican Rds

c

St & NORTRN lines

Burlington Northern

Santa Fe

BEFORE THE SENATE COMMITTEE ON SMALL BUSINESS

AND THE HOUSE OF REPRESENTATIVES

COMMITTEE ON SMALL BUSINESS

JOINT HEARING ON

RAILROAD CONSOLIDATION: SMALL BUSINESS CONCERNS

STATEMENT OF SAVE THE

ROCK ISLAND COMMITTEE, INC.

James Link
Vice Chairman
Save the Rock Island
Committee, Inc.

Dated: November 20, 1995

BEFORE THE SENATE COMMITTEE ON SMALL BUSINESS

AND THE HOUSE OF REPRESENTATIVES

COMMITTEE ON SMALL BUSINESS

JOINT HEARING ON

"RAILROAD CONSOLIDATION: SMALL BUSINESS CONCERNS"

STATEMENT OF SAVE THE
ROCK ISLAND COMMITTEE, INC.

The Save the Rock Island Committee, Inc. ("STRICT"), submits this statement for inclusion in the record for the joint hearing held before the House and Senate Committees on Small Business on November 8, 1995, on "Railroad Consolidation: Small Business Concerns." STRICT is a not-for-profit Missouri corporation formed in early 1994 for the express purpose of first preventing the abandonment and further deterioration and then securing the reactivation of the rail line that runs across the state of Missouri between the Kansas City and St. Louis areas. The line is now owned by the St. Louis Southwestern Railway Company ("SSW"), a subsidiary of the Southern Pacific Rail Corporation ("SP"). A list of the Board of Directors of STRICT is attached hereto as Appendix 1.

Because STRICT was formed in large part by and for small agricultural and manufacturing businesses, STRICT believes that it would beneficial to share with the committees its recent experiences with SP and SSW, both before

and after SP announced its intention to merge with the Union Pacific Railroad Company ("UP").

It is the goal of STRICT, which is composed of rail shippers, potential rail shippers, and local government agencies representing them and the interests of the general public in central Missouri counties, cities and communities between Kansas City and St. Louis, that the rail line in question be operated in its entirety, as was promised when SSW purchased the line in 1980. For nearly two years, STRICT has been active on multiple fronts to accomplish that objective, in order to further the cause of economic development in central Missouri. With cooperation from the owning railroad, achieving the goal would not be that difficult. Instead, STRICT has been met at almost every turn with ambiguity, obfuscation and frequently shifting positions. The Interstate Commerce Commission ("ICC") has been reluctant to come to grips with the problems STRICT has encountered.

STRICT's experiences have led it to draft proposed legislation. STRICT urges that its proposed merger provision be included in the Interstate Commerce Act amendments now under consideration by the Senate.[1] A discussion of the suggested provision is included in this statement. It is STRICT's hope that the members of the Small Business Committees will urge other Senators and Representatives to adopt such language as part of the pending bills to transfer certain of the functions of the ICC to a successor agency.

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[1] S. 1396, The Interstate Commerce Commission Sunset Act of 1995, is likely to be considered in the near future by the Senate; H.R. 2539, The ICC Termination Act of 1995, was passed by the House on November 14, 1995. It is clear that due to the differences between these bills, further action to resolve the differences will occur, and so there will be opportunities in the Senate as well as in Conference Committee to adopt the STRICT legislative proposals.

BACKGROUND

SSW's cross-state line was one of Missouri's most significant rail lines. Connecting the important rail gateways of Kansas City and St. Louis, it runs through many communities that have no other opportunity for direct rail service. Unfortunately, the line was previously owned and operated by the Chicago, Rock Island, and Pacific Railroad Company ("Rock Island"), which went bankrupt and was liquidated. During the 1960's and 1970's, the Rock Island's financial condition was such that it could not adequately serve its customer base or maintain its physical plant. Consequently, rail shippers did not receive proper service and drifted away from the subject rail line. The line's physical condition deteriorated due to lack of maintenance, which resulted in an even greater loss of traffic. The Rock Island eventually ceased operating the line in the late 1970's, following bankruptcy. The line was slated for liquidation as part of the Rock Island bankruptcy proceedings.

While a number of Class I carriers expressed interest in acquiring the line, the trustee of the Rock Island estate chose to sell it, along with other Rock Island rail lines outside of Missouri, to SSW. The State of Missouri strongly supported SSW's acquisition of the line because of the essential services provided by the line.

The importance of Rock Island's St. Louis to Kansas City line was affirmed in the application which SSW filed with the ICC to purchase the line.[2] Further affirmation came when Missouri Pacific Railroad Company ("MP") filed a competing application with the ICC to acquire the line. During the ICC application process, MP stated that 8,000 carloads of traffic had

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[2] See St. Louis Southwestern Railway Co.--Purchase (Portion)--William M. Gibbons, Trustee of the Property of Chicago, Rock Island and Pacific Railroad Co., Debtor, 363 I.C.C. 323 (1980).

originated from or terminated at the various stations on the line in the last full year the line was operated by Rock Island.

Because of the competing applications, the ICC was forced to compare SSW's application with MP's application, and was obligated to grant that application which would best serve the public interest in assuring rail service over the line. While both carriers promised to provide local service, in urging the ICC to grant its application SSW went so far as to claim that it would provide local service <u>even if it were to obtain trackage rights and thus be able to route overhead traffic over another line</u>. SSW also stated that it would not abandon the former Rock Island line for at least ten years. Such promises proved empty.

Soon after the ICC granted its application and SSW purchased the line, SSW, in response to the merger application filed with the ICC by MP, UP, and Western Pacific Railroad Company, requested that the ICC, as a condition to any approval of that merger, require that SSW be granted trackage rights over roughly parallel MP lines between Kansas City and St. Louis.[3] The lines are a relatively short distance north of the former Rock Island line. In so requesting, SSW stated to the ICC that such trackage rights would save it approximately $77 million. That was SSW's estimate of the difference in cost for upgrading the former Rock Island line from Federal Railroad Administration ("FRA") Class 2 standards for local traffic to FRA Class 4 standards, which SSW claimed would be necessary to allow the line to operate at faster speeds for handling overhead traffic. Since obtaining the trackage rights would

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[3] <u>See</u> <u>Union Pacific Corp., Pacific Rail System, Inc., and Union Pacific Railroad Co.--Control--Missouri Pacific Corp. and Missouri Pacific Railroad Co.</u>, 366 I.C.C. 462 (1982), <u>aff'd</u> <u>in</u> <u>part</u> <u>and</u> <u>remanded</u> <u>in</u> <u>part</u> <u>sub</u> <u>nom</u>. <u>Southern Pacific Transportation Co. v. ICC</u>, 736 F.2d 708 (D.C. Cir. 1984), <u>cert</u>. <u>denied</u>, 469 U.S. 1208 (1985).

enable SSW to forego overhead traffic over the line it owned, SSW would only incur costs for maintaining its line to Class 2 standards.

In order to preserve competition in the nation's important central rail corridor, the ICC granted the trackage rights requests of a number of carriers in the UP-MP merger case, including SSW's request for trackage rights over the MP lines in Missouri. The ICC stated that it was granting SSW trackage rights over the MP lines in order to allow SSW immediate access between Kansas City and St. Louis and to enable SSW to avoid the aforementioned expense of upgrading the former Rock Island line.

To the great detriment of many communities along the line, SSW, in the fifteen years it has owned the former Rock Island line, has never provided rail service, local or otherwise, over much of the line. Very little if any of the rehabilitation promised by SSW, even for local service, ever took place.

Instead, as soon as SSW took possession of the line, it embargoed the 196.7 miles between Owensville, MO, and the point at which the line terminates in the Kansas City area, Leeds Junction, MO. While embargoes are defined by the ICC and the courts to be temporary emergency measures,[4] SSW's embargo has never been lifted.

In addition, even though the eastern 81 miles of the former Rock Island line have been operated by SSW, in recent years a large surcharge on shipments originating or terminating west of Union, MO, has resulted in a precipitous decline in traffic on the 32 miles of the line covered by the surcharge. Thus, for all intents and purposes, under SSW's lackluster stewardship the

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[4] See, e.g., ICC v. Baltimore and Annapolis Railroad Co., 398 F. Supp. 454 (D. Md. 1975), aff'd 537 F.2d 77 (4th Cir.), cert. denied, 429 U.S. 859 (1976); Overbrook Farmers Union Cooperative Association--Petition for Declaratory Order--Violation of 49 U.S.C. § 11101(a), 5 I.C.C.2d 316 (1989).

former Rock Island line between Kansas City and St. Louis has been reduced to a 50-mile branch line extending from the St. Louis area, while the remainder of the line has been permitted to deteriorate to an even worse state than when Rock Island owned it.

It should be noted that Missouri is a state in which the great preponderance of rail traffic is overhead traffic. Little more than one quarter of the loaded rail cars that move through Missouri originate from or terminate at points in the state. The large rail carriers increasingly consider most of Missouri simply as scenery, as most of their trains travel without providing any local service between major cities such as Kansas City, St. Louis, and Chicago. Reactivation of the former Rock Island line between St. Louis and Kansas City would give rise to the opportunity for local shippers to use rail service again or at an increased level. It would begin to reverse the trend of economic withering experienced by so many communities. Would new industry locate along the line? <u>You bet</u>! Just think of the situation involving location of the new Mercedes-Benz plant in rural Tuscaloosa County, AL. Had the rail line that will serve that plant been abandoned, would Tuscaloosa have been seriously considered for this major industrial plant that will depend on rail service? <u>No way</u>.

After never having operated much of the line in dereliction of the multiple promises made in regulatory proceedings - it welshed on every promise made to local and state interests on the point - SSW on October 19, 1993, filed a Notice of Exemption with the ICC to abandon the 196.7-mile line segment between Leeds Junction and Owensville. It was in response to that filing that interested parties came together to ultimately form STRICT.

While that Notice of Exemption was automatically effective on November 18, 1993, SSW could not consummate the abandonment because of the interest at

that time shown by parties to purchase all or some of the line segment.[5] In the meantime, STRICT, on January 12, 1994, filed a request that the ICC declare the entire abandonment exemption void ab initio because of patently false information contained in the SSW filing with the ICC. The ICC agreed with STRICT and issued a decision which revoked SSW's abandonment.[6]

With its request to void the exemption, STRICT filed a complaint against SSW with the ICC. The complaint was based upon SSW's unlawful refusal to provide rail service over the former Rock Island line, SSW's responsibility for unlawful impediments to such service, and SSW's illegal embargo of service

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[5] That interest soon dissipated, however, to the extent that only UP was interested in purchasing the approximately 25 miles of line between Pleasant Hill, MO, and Leeds Junction.

[6] See ICC Docket No. AB-39 (Sub-No. 18X), The St. Louis Southwestern Railway Co.--Abandonment Exemption--In Gasconade, Maries, Osage, Miller, Cole, Morgan, Benton, Pettis, Henry, Johnson, Cass, and Jackson Counties, MO (not printed), served April 1, 1994. STRICT also opposed before the ICC an unsuccessful request by SP for expanded and extended trackage rights for SSW over the MP Lines in Missouri, a request made in response to UP's application to the ICC to control the Chicago and North Western Transportation Company and its railroad subsidiary. See ICC Finance Docket No. 32133, Union Pacific Corp., Union Pacific Railroad Co. and Missouri Pacific Railroad Co.--Control--Chicago and Northwestern Transportation Co. and Chicago and North Western Railway Co., slip. op. served March 7, 1995. Finally, STRICT has petitioned the ICC to reopen the proceeding in which the ICC decided that SSW should be granted trackage rights over the MP lines in Missouri. STRICT's goal in so doing is to have those trackage rights revoked and SSW left with no direct route between Kansas City and St. Louis other than the former Rock Island line, in order to increase the probability that the former Rock Island line would be operated in its entirety. That petition, filed June 13, 1994, remains pending before the ICC. Of course, now UP and SP are proposing to merge, which would again make the old Rock Island line between St. Louis and Kansas City about as wanted as the proverbial red-headed step child at a family reunion. But rather than sell the line as a unit, they would apparently rather chop it up. Certainly that remains the position of SP. The position of UP remains to be fully seen, although STRICT hopes that something can be worked out that will resolve all of its concerns.

on, and unlawful abandonment of, the Leeds Junction-Owensville segment of the line.[7]

The ICC eventually accepted STRICT's amended complaint and established separate complaint proceedings for the Leeds Junction-Owensville line segment and the remainder of the former Rock Island line. The first part of the bifurcated complaint proceeding was consolidated with SSW's renewed request for an exemption to abandon the line segment.[8]

Before the discovery phase of either complaint proceeding progressed very far, representatives of STRICT and SP met in September of 1994 to discuss how further litigation could be avoided. Since that meeting, the complaint and abandonment proceedings have been held in abeyance by the parties in order to determine whether a suitable short line operator for at least part of the former Rock Island line can be found. While STRICT's position continues to be that SSW is obligated to operate the line, STRICT's primary objective is the reactivation of rail service over the entire line, and thus it supports sale of the line to any responsible operator that will provide local service.

Consequently, since last fall STRICT has been encouraging parties interested in providing service between Kansas City and St. Louis to negotiate with SSW. It is STRICT's position, as well as that of the potential railroad operators with which it has discussed the matter, that for a new operator on the former Rock Island line to succeed, it will have to be able to operate over the entire line between St. Louis and Kansas City, with freedom to

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[7] The complaint was amended on March 8, 1994, to include MFA Incorporated ("MFA") as a complainant. MFA is a farmer-owned cooperative association and agricultural services company with members in most if not all of the communities located along the former Rock Island line. MFA also has its own shipping and receiving facilities located on numerous points on the line.

[8] See ICC Docket No. 41195, Save the Rock Island Committee, Inc., and MFA Incorporated v. The St. Louis Southwestern Railway Company (not printed), served July 19, 1994.

interline at each end without restriction. The benefits of doing so are obvious, given the number of large carriers whose expansive rail systems serve those two points.

One company in particular, General Railway Corporation ("GRC"), of Omaha, NE, has worked closely with STRICT on an acquisition proposal. STRICT supports GRC because, to this point, GRC is the only potential short line operator that has made concrete and viable proposals to rehabilitate and operate the line between St. Louis and Kansas City. GRC, which was formed by experienced railroaders, made what was thought to be significant progress towards reaching an agreement in principle with SSW following extended negotiations in late 1994 and the first half of 1995.

Despite all those months of negotiation, however, SSW's parent, SP, has thus far refused to enter into any agreement which would allow GRC to establish a short line railroad that could operate between Kansas City and St. Louis. At first, SP indicated that it would agree to sell or lease the largely inactive segment of the former Rock Island line to GRC, but objected to selling the eastern 35 miles of the line between Labadie, MO, and St. Louis, or even granting the purchaser overhead trackage rights so that the trains of the new carrier could operate between St. Louis and Kansas City. It also refused to even consider allowing GRC rights to serve the facilities of Union Electric Company near Labadie, MO.

Now, beginning around the time that UP and SP announced their intention to merge on August 3, 1995, SP has taken the position that it will also not sell to GRC the western 25 miles of the line between Pleasant Hill, MO, and Leeds Junction, but would rather sell that segment of the line to its merger partner, UP. SP's position is that it will only permit the sale of the center

part of the line, which even a layperson could see would never survive as an independent railroad.

If SP is successful in implementing its foregoing plan, the consequences are clear. While SP in its application in 1980 to acquire the former Rock Island line stressed the need to be able to operate between Kansas City and St. Louis, it is now actively trying to prevent the line from being used by any other one carrier in such a fashion. Thus, at a time at which the large Class I carriers in the country are merging in order to increase the size and scope of their rail systems and become more efficient, SP is trying to dismember one of the more direct rail lines that connect the important rail gateways of Kansas City and St. Louis.[9]

The only conclusion that can be drawn from these circumstances is that SP is fearful that the former Rock Island line will be used to provide competitive rail service in that corridor, and is acting to prevent that from happening. Given SSW's failure to keep the commitments it made with respect to the former Rock Island line, that is nothing short of tragic for the many communities through which the line runs.

In light of the clear connection between SP's conduct and its plans to merge with UP, STRICT has become involved in the UP-SP merger proceeding before the ICC. While further litigation is the last thing STRICT wants, SP's actions have left it no choice but to try to rectify in the UP-SP merger proceeding the 15 years of injustice that have resulted from SSW's

---

[9] It is STRICT's information that the only shipper on the line whose traffic level is presently large enough to justify continued local rail service by a high-cost carrier such as SSW is the Union Electric Company power plant at Labadie, MO. As UP already provides the bulk of service to Union Electric there, after the merger there will be no need for separate SSW service to that location.

mistreatment of the shippers and communities along the former Rock Island line.

THE NEED FOR LEGISLATION

Should SP continue with its present course of conduct, and refuse to negotiate reasonable terms for an agreement which would allow rail operations to be conducted by a short line carrier between Kansas City and St. Louis over the former Rock Island line, it is STRICT's intention to request the ICC or its successor agency to condition any approval of the UP-SP merger on sale of the entire line to GRC or some other competent operator truly committed, unlike SSW, to providing local rail service. Imposition of such a condition is only equitable in light of the actions of SSW and its parent, SP, over the past 15 years, and most especially over the last two years.

While the Interstate Commerce Act as it now exists is quite susceptible to being interpreted to permit such a condition to be attached to a merger of two Class I carriers, the ICC's conditioning authority is in large part permissive. Moreover, when the ICC is abolished and its duties taken over by the proposed Transportation Adjudication Panel ("TAP")[10], STRICT is concerned that TAP will continue the implementation of the restructured Interstate Commerce Act in such a way as to favor the goals of large railroads rather than to look out for the interests of STRICT and its members. Given the discretion that the ICC has and that TAP will have, it would be a simple matter for that discretion to be used to find, for example, that an insufficient record has been presented to warrant the imposition of any

[10] S. 1396 names the ICC's successor the Intermodal Surface Transportation Board, but since H.R. 2539 has already passed the House, the name in the latter bill is generally used when referring to the successor agency.

conditions such as would protect the viability of the St. Louis-Kansas City line, almost regardless of what that record would contain. It is also quite expensive for parties interested in preserving rail lines to become involved in large carrier merger proceedings in order to build a record. Such proceedings can become quite complicated and thus can require much in the way of expensive studies and evidentiary presentations if a serious attempt is to be made to convince the ICC to exercise its discretion in a favorable way.

As a result of knowing how the ICC has handled such matters in the past, STRICT urges Congress to include in the pending legislation which would terminate the ICC and transfer its various functions an amendment which would require the successor to the ICC to adequately address in the UP-SP merger proceeding what is happening in the case of the former Rock Island line and what is bound to occur elsewhere in the future as a result of mergers between large rail systems. STRICT has suggested the following language to the Senate Commerce Committee[11] as a new subsection (d) to be added to existing Section 11344 of Title 49 of the United States Code:

> (d)(1) In a proceeding under this section which involves the merger or control of at least two Class I railroads, as defined by the Transportation Board, the Transportation Board shall condition its approval upon divestiture of a line or lines of an applicant when it finds the following:
>
> (A) The line is essentially duplicative of or parallel with another line that will be owned by an applicant or a carrier under common control or commonly controlled with such applicant;
>
> (B) Without overhead traffic, the entire line as a unit may not be economically viable;
>
> (C) Abandonment of the line, were it to take place, would impede rural economic development or have an adverse impact upon small business interests;

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[11] The proposed legislation refers to the successor agency as the Transportation Board, consistent with the language of S. 1396.

(D) The line is shown on the System Diagram Map in Category I or II, or there has been an attempt during the preceding five years to abandon any part of the line, or there is a reasonable likelihood that the line may be abandoned within five years after consummation of the proposed transaction; and

(E) Interested shippers or governmental bodies seek to have the condition imposed, or a potential purchaser seeks to buy the line in a responsive application.

(2) In the event of multiple offerors, the Transportation Board shall choose the most qualified offeror not affiliated in any manner with an applicant.

(3) The purchase price for the line shall be set at a net liquidation value to be mutually agreed upon or failing that one set by the Transportation Board following submission by the parties of valuation evidence.

(4) In setting time limits for consummation of divestiture, the Transportation Board shall allow adequate time for completion of financing arrangements, which may be extended upon the request of a proposed transferee. In the event of multiple offerors, should the chosen offeror not be able to consummate the proposed transaction, then the Transportation Board shall allow the next most qualified offeror to acquire the line being divested under the same terms.

(5) No purchaser of a line or portion of line sold under this section, or its successor, may discontinue service on such line prior to the end of the second year after consummation of the sale.

(6) This subsection shall be applicable to proceedings pending on the effective date of this act where the time for filing responsive applications has not expired.

The suggested amendment, while limited to carefully circumscribed situations, would direct the successor to the ICC to remedy a clear harm to rural America resulting from the merger of large rail carriers.

Among other reasons, carriers such as UP and SP merge in order to achieve what are known as economies of density. That is, to be more efficient, and thus to better compete on both an intramodal and intermodal

basis, large rail carriers need to increase their asset utilization rates by routing more traffic on fewer lines. Hence, as the result of the merger between UP and SP, traffic formerly carried on the line of one or the other will eventually be rerouted over the line that is more efficient for that traffic.

In the case of lines that are parallel for long distances, it is quite likely that after the merger the combined carrier will eventually use only one of the lines, rendering the other redundant, at least for the merged carrier. Local shippers and the economic development prospects of communities along the unwanted line could very well be dependent on that line, but the newly merged carrier will have little interest in operating it without overhead traffic.

At the same time, however, the merging carriers may not want the line to be operated by another carrier, since the line could be used in competitive rail routings. The line will thus not be voluntarily sold to a party interested in operating it, nor will it be abandoned all at once, as the carrier could then be required to sell it to a new operator at its net liquidation value under present 49 U.S.C. Section 10905.[12]

Instead, and in order to render the line noncompetitive with other rail lines, it has been the practice of most Class I railroads to abandon an otherwise desirable line in segments. A rail line's transportation value is based in large part on the points it connects. By abandoning only one part of the line, and thus isolating the active part of the line from one of the important points previously served, the carrier will discourage interested parties from stepping forward to purchase the line segment. Purchasers are

---

[12] STRICT is concerned that under proposed revisions to abandonment law contained in H.R. 2539, it will be much easier and faster to abandon a line of railroad than in the past, making enactment of the legislative language it proposes even more urgent.

thus discouraged because the costs of providing rail service over the line are increased due to the fact that it is necessary for two carriers - the purchasing carrier and the existing carrier - to provide service over a route which previously was served by only one carrier. Such an increase in costs is axiomatic.

Ironically, the dismembering of potentially viable rail lines is occurring at the same time that large Class I carriers are merging their already large systems in order to connect routes previously served by separate carriers. By eliminating the need of the two carriers to interline traffic, the merging carriers claim that they will create "seamless" and thus more efficient service. Logic dictates that if large carriers are going to be permitted to merge in order to provide extended single line service, at the same time they should not be permitted to chop up a parallel line they don't really intend to operate in order to keep it out of the hands of an operator that would like to continue to operate it as a unit. Such chopping up of the spaghetti of the national rail system so as to prevent an affected line from being operated as a unit is a clear precursor of further abandonments and is in clear derogation of the public interest in an efficient and competitive rail transportation system.

STRICT believes that a more proactive stance, legislatively directed, is necessary if businesses along an affected line are not to be adversely affected. In many instances, by the time a carrier proposes to abandon a line, a number of the shippers have already been discouraged from using the line and have ceased using rail service. Operation of the line is therefore less attractive to a new operator, and thus it is less likely that a new operator will be interested in purchasing it. Clearly, action must be taken

at an earlier point in time to preserve such a rail line for its patrons and prospective patrons.[13]

As alluded to earlier, one large cause of rail line abandonments is mergers between rail carriers whose systems run at least partially parallel with each other. As can be seen from any rail map of the western two-thirds of the United States, UP and SP have rail lines that in some cases are parallel for hundreds of miles. Consequently, it can be expected that some such lines will be abandoned in coming years if the merger occurs. Indeed, UP and SP have identified several hundreds of miles of rail lines that they plan to propose to abandon in connection with the merger proceeding. Interestingly, many of these lines slated for abandonment are middle segments of much longer lines.

There is, therefore, a timely need for the proposed amendment. The amendment would only apply in the case of the merger of two Class I rail carriers, as has been proposed with UP and SP. There are now only nine such rail carriers left in the country, whereas a decade ago there were many more. Because the UP-SP merger will cause that number to decrease even further, the amendment has been drafted to apply to the UP-SP merger.

The amendment is mandatory, in that the ICC's successor would have to order divestiture of a line if the several listed conditions are met. This is necessary because the ICC has shown little inclination in recent years to prevent carriers from structuring abandonments to stifle rail competition.

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[13] STRICT applauds the action of the House in H.R. 2539 in restoring the feeder railroad provisions currently found in 49 U.S.C. § 10910 to the bill as it was finally passed. But such provisions provide only a partial solution to the problem of preservation of feeder railroad lines, and their use is especially problematic in a merger case. That is why the suggested language or something of similar effect is essential.

At the same time, it will be up to the ICC's successor agency, employing its expertise in such matters, to make the required findings under proposed subsection 11344(d)(1). Divestiture will be required of a line only if the line is parallel with or duplicates another rail line involved in the merger, and there is a reasonable likelihood that the line may be abandoned in the next five years. Of course, if there has been a recent attempt to abandon the line, or if the line is already identified as a Category I or Category II line, meaning that the owning carrier believes the line to be a candidate for abandonment, there is no reason for the ICC's successor to look any further for evidence that the line will be abandoned as a result of the merger.

The ICC's successor will also need to make requisite findings regarding the economic viability of the line absent overhead traffic and the effects of abandonment with respect to rural economic development and small businesses. Finally, even if the all of the foregoing findings are made, divestiture will not be automatic. Divestiture must be requested by either interested shippers or governmental bodies, or there must be a responsive application filed by a potential purchaser.

The remainder of the amendment is similar to provisions presently contained in the Interstate Commerce Act which require carriers to divest rail lines in certain instances, specifically 49 U.S.C. Section 10905, known as the offer of financial assistance statute, and 49 U.S.C. Section 10910, the feeder railroad development statute. Under the terms of the amendment, the purchase price is the line's net liquidation value ("NLV"), because the ICC has previously found that a line which is likely to be abandoned has no value greater than its NLV.[14] If the selling carrier and the purchaser cannot agree

[14] See Chicago and Northwestern Transportation Co.--Abandonment Between Ringwood, IL and Geneva, WI, 363 I.C.C. 956 (1981), aff'd, 678 F.2d 665 (7th Cir. 1982).

on the line's NLV, the ICC's successor is empowered to determine the line's NLV.

The proposed language prohibits the purchaser of a line from discontinuing service over the acquired line for at least two years. This requirement should ensure that only those parties truly interested in operating the rail line in question invoke the terms of the amendment to Section 11344.

Some of the features of the amendment do differ from 49 U.S.C. Sections 10905 and 10910. Under proposed Section 11344(d)(2), if more than one party wishes to acquire the same rail line, the ICC's successor agency is required to choose the most qualified offeror not affiliated in any manner with one of the merger applicants. Section 10905(f)(3) presently permits the selling carrier to choose the party with which it will deal, and the ICC has interpreted 49 U.S.C. Section 10910, which is silent on the subject, in an identical manner.[15]

The selling carrier, however, can hardly be expected to be impartial in its choice of purchasers. By granting the power to choose among multiple offerors to the ICC's successor, Congress can be better assured that the offeror which can provide the strongest competition to the selling carrier will be granted the right to purchase the entire line.

Proposed Section 11344(d)(4) also grants to the purchaser of a line a reasonable amount of time to obtain financing. In the case of any rail line

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[15] See Cheney Railroad Co.--Feeder Line Acquisition--CSX Transportation, Inc. Line Between Greens and Ivalee, AL, 5 I.C.C.2d 250 (1989), review denied, 902 F.2d 66 (D.C. Cir.), cert. denied, 498 U.S. 985 (1990). This shows how an abuse can be perpetrated which destroys the utility of a line by selling a short portion of it to a collusive purchaser. Unfortunately, this was sanctioned by the ICC, and so gives additional urgency to enactment of legislative language to prevent it from happening in connection with a merger proceeding.

sale that is less than totally voluntary, and in which the terms and conditions of the sale are not certain until such time as the ICC establishes those terms and conditions, potential purchasers are bound to face more difficulties in obtaining financing than in the case of a voluntary sale at an agreed price. Financing sources are notoriously leery of any project in which there is the slightest unresolved issue, and thus would be far more likely to deal with a party acquiring a rail line only after issues impacting the sale, including purchase price, have been decided. Thus the amendment provides additional time for purchasers to secure financing for such transactions, and further provides that in the case of multiple offerors for a line, if the party originally chosen to acquire the line cannot consummate the transaction, the ICC's successor will designate another purchaser from among the interested parties.

While STRICT believes that the amendment as drafted has much to commend it, STRICT is of course open to suggestions from members of the committees and their staffs regarding any modifications. However, STRICT wants to reiterate the urgent need for legislation to address matters at an early date. For any further information, or if there are any questions, STRICT can be contacted through its transportation counsel, William P. Jackson, Jr., of Jackson and Jessup, P.C., Post Office Box 1240, Arlington, VA 22210. Mr. Jackson's phone number is (703) 525-4050, and his telecopier number is (703) 525-4054.

James A. Link
James Link
Vice Chairman
Save the Rock Island Committee, Inc.

SAVE THE ROCK ISLAND COMMITTEE, INC.

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Appendix 1

ARIZONA GRAIN, INC.
VALLEY SEED
A DIVISION OF ARIZONA GRAIN INC

P O BOX 11188
CASA GRANDE. AZ 85230-1188

TELEPHONE 602-836-8228
FAX 602-421-0832

November 6, 1995

The Honorable Christopher Bond
Chairman
Senate Committee on Small Business
428 A Russel Senate Office Building
Washington, DC 20510

Dear Chairman Bond:

The joint House Senate Business Committees hearing on the impact of railroad mergers on small business leads us to request the following information be made available to the committee members and staff, and be included in the permanent hearing record.

As president of Arizona Grain, Inc. of Casa Grande, Arizona, I appreciate this opportunity to express the Company's views on the proposed merger of the Union Pacific and Southern Pacific railroads.

Arizona Grain, Inc. is one of Arizona's largest grain handling companies with grain facilities in Casa Grande, Buckeye, Roll, and Yuma, Arizona. The Company ships and receives over 3,000 railcars per annum on the Southern Pacific Railroad. The Company's products that it ships or receives via it's railroad service includes durum wheat, milling red wheat, feed wheat, barley, corn, and milo. The Company exports wheat via the Houston and Corpus Christi, Texas grain export facilities and originates most of its feedgrains from Kansas, Oklahoma, Nebraska, and Iowa.

Arizona Grain, Inc. strongly supports the merger of the Southern Pacific and Union Pacific railroads. We view the merger as one that will bring the following benefits:

- Improved Service: SP's limited resources has resulted in inconsistent service levels for our business over the past several years. UP has an excellent background of service performance that will aid us in meeting our customer needs. With current SP performance it will be difficult to remain competitive within our marketing area.

The Honorable Christopher Bond
Page 2

- Expanded Grain Origination: SP's limited origination base for feed grains has restricted Arizona Grain's ability to provide product for the local market.

  Arizona Grain will now have single line access to Nebraska and Iowa grain sources as well as vastly expanded access to Kansas and Missouri origins.

  With single line access to UP/CNW's vast origination base for feed grains we feel we can now be competitive in addition to providing the local feeding industries a much need lower delivered cost for their feed grain needs. For example, the combination of UP/SP will give local feeders single line access to lower priced Iowa corn from CNW origins. This scenario will encourage additional expansion in both the local beef and dairy industries which are primary customers of our business.

- Equipment Utilization: Opportunities exist for better utilization of equipment with reload potential for many of the west bound covered hoppers with east bound wheat to points in the Texas gulf and to midwest and east coast mills. This will help to alleviate current car shortage problems being experienced by Arizona Grain on the SP. Equipment supply has been a limiting factor in expanding local production of high quality durum wheat for foreign and domestic millers.

- More Market Opportunities: A merged UP/SP will provide additional single line markets for Arizona's high quality durum wheat. Markets in Minnesota and Illinois will be accessible via a single line route where in the past they have been only available on a joint line basis. We believe single line pricing will allow us more competitive access into these markets.

From our standpoint, it is important to see two strong rail systems in the west, and to be served by one of them, than to try to preserve three railroads with one being an independent but weaker SP in the present railroad environment. More of the same will not allow Arizona Grain and or the industries we serve to grow and expand in the future.

The Honorable Christopher Bond
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We support the ICC on its suggested fast approval of the merger so as to expedite the combining of these very important railroads.

Thank you for the opportunity to address my views to this committee.

John Skelley

John Skelley
President
Arizona Grain, Inc.

11-7-95
Date

Farmers Elevator Association of Minnesota

Since 1907

JOINT HEARING
SENATE/HOUSE SMALL BUSINESS COMMITTEE
WEDNESDAY, NOVEMBER 8, 1995

Dear Chairman and Members of the Committee:

My name is Bob Zelenka, Executive Director of the Farmers Elevator Association of Minnesota, a 400 member grain elevator trade association. A recent conversation with Senator Wellstone concerning rail issues led to his invitation to address some of these concerns with this Small Business Committee.

Our average member handles 2.2 million bushels of grain, employs 11 people and does about $9 million is sales annually. The large majority are termed small agri-businesses and are an integral part of hundreds of rural communities. This year, our rail user member have experienced one of the worst years in memory, in terms of rail service and pricing. You are probably very familiar with the problem we've had with getting cars and the untimely rate increases we've experienced so I won't dwell on it. However, the railroad mergers that have occurred, along with the extensive railroad efforts to effectively eliminate nearly all regulatory oversight is extremely troubling, especially to the small to medium rail user. For example, a House bill (HR2539) that may go to the floor next week has, in our opinion, many shortcomings. Among our concerns, the House bill:

1. Eliminates current contract protections for shippers/receivers; no contract filings mandated; no limitation on percentage of cars that can be devoted to contract service (current law says 40% maximum); and eliminates current prohibitions against discriminatory contracting (under current law, if you can offer similar circumstances and assurances to a carrier, they are required to offer similar terms).
2. Circumvents any common carrier obligation by permitting all cars to be committed to contract service (see above);
3. Eliminates the 20-day notice requirement to effect rate increases or substantive changes in terms of tariff carriage;
4. Eliminates the right of rail users to object to rail line abandonment applications and challenge rail mergers;
5. The House bill also makes it easier for carriers to obtain exemptions for certain classes of traffic (export corn/soybeans is being considered), and does nothing to permit shippers to challenge unreasonable actions by railroads in court. When an exemption is granted, it continues to be an almost impenetrable cloak of protection for the railroads.

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We strongly support continuation of oversight and encourage support of the Pressler-Exon Senete bill (S.1396). While we would be the first to admit that the Interstate Commerce Commission has been ineffective in its oversight duties, we now have an opportunity to develop a "meaner and leaner" oversight agency that can conduct the hard analysis of impacts of rail mergers and offer safeguards to rail users related to railroad practices. Now is not the time to abandon small businesses, who are at the mercy of practices under a near monopoly situation.

Thanks you for your kind consideration and please contact me if more details would be desired

Farmers Elevator Association of Minnesota

Since 1907

August 25, 1995

The Honorable Paul Wellstone
717 Hart Senate Office Bldg.
Washington, DC 20510

Dear Senator Wellstone:

The grain industry has been experiencing a recent crisis in the area of grain transportation, both in terms of availability and cost. Barge, rail and truck transportation is historically tight around this time, but this year has been exceptionally bad.

A lot of rail traffic (grain) was moving to the west coast, with a majority of that traffic going through a terminal elevator in Tacoma Washington. Unfortunately, an elevator explosion at the facility on July 22 closed down the facility and traffic had to be diverted, increasing the time it takes to unload cars and return them for re-use. This bottleneck slowed rail movements way down and made availability even more of a problem than usual. To compound the problem, both the Burlington Northern and Soo Line implemented a freight rate increase in early August that caught many grain elevators off guard. The increase had the appearance of profiteering by the railroads due to the tight supply. Many elevators had already contracted with producers for fall delivery based on the existing freight costs, so this unexpected increase with less than 30 day notice, cut directly into the margin built into the contract and left many elevators losing money on many transactions. A recent survey by our Association indicated that elevators are facing upwards of $400,000 in additional freight costs, with much of that being absorbed by elevators who operate on slim margins to begin with.

The barge situation on the Mississippi and Minnesota rivers has also added to our current transportation crisis. The cost of barge freight got as high as 415% above tariff, which led to an availability problem because terminals were unwilling to pay the price. Again, the perception of profiteering by barge companies was echoed by many of our county elevator members, who found themselves unable to move much grain out of the elevator or to even handle grain coming in off the farm. Is this as simple as supply and demand related pricing or is there more to the story?

My point of this correspondence is to let you know how important it is to have some form of independent third party oversight over these transportation carriers. We function at their mercy and now is not the time to totally move away from a regulatory oversight process. The current effort to eliminate the Interstate Commerce Commission (ICC) has been very disconcerting. While the ICC has been ineffective in some of its functions, the need for an effective form

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of regulatory oversight is probably more important today than ever. With railroad mergers, the number of firms competing are reduced thus increasing the concern over anti-trust situations. The barge companies seem to have free reign to set prices at whatever the market may bear. Who's minding the affairs of the barge firms for the public good? We have country elevators that are facing $20,000 to $200,000 in additional barge freight costs, some of which cannot be passed on to producers and must be absorbed by the country elevator. This has also impacted the cost and availability of grain truck transportation moving to the rivers, which has slowed down as well.

I'd like to encourage you to take a serious look at the Senate version of the ICC legislation and consider a less drastic cut in its funding. Further, I'd encourage you to join Senator Exon in Promoting (S.1140), legislation that would eliminate the ICC but vest future regulatory authority over rail transportation within an independent board at the U.S. Department of Transportation.

Should Congress proceed to adopt deficient appropriations legislation, it may be in the best interests of the grain, feed and processing industry to explore new, novel remedies to protect rail grain users. Among the options that may warrant serious consideration are the following:

- Vest federal and/or state courts with original jurisdiction over all actions involving rail carriers, regardless of whether the given rail activity is regulated. Congress could instruct courts to resume the role they had prior to enactment of the Interstate Commerce Act, when federal common law applied to all matters involving rail carriers. Under this option, rail users would have the right to seek redress against unreasonable rail practices in the courts.
- Vest in the U.S. Department of Agriculture the authority and responsibility for filing rail tariffs and summaries of rail contracts involving agricultural commodities and byproducts. Conceivably, USDA also could be granted authority to intervene on behalf of agricultural rail users and rural communities to protect rail line abandonments.
- Limit DOT's role to jurisdiction over rail line abandonments and filing of rail car liens.

I hope you can appreciate how much decisions by transportation carriers can impact the entire agriculture industry and why some oversight is needed. Your understanding and support in this vital area would certainly be appreciated.

With Best Regards,

Bob Zelenka

Bob Zelenka
Executive Director

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Sunday, October 29, 1995

Business

Railroads of future expected to be huge
Anthan George
Washington News Bureau

Washington, D.C. - Within five years, rail transportation in the western half of the United States will be controlled by two mega-railroads, and in the East two others are expected to be the dominant ones.

Despite the emergence of a few huge railroads and concerns from some customers and from some local officials about the potential for unfair rates, a member of the Interstate Commerce Commission is not worried.

"I don't see a rebirth of the robber barons," Commissioner Gail McDonald said.

Linda Morgan, the ICC's chairwoman, agreed: "Rail people are top business people, much more sensitive to shippers."

Congress is expected to abolish the Interstate Commerce Commission and hand some of its functions to the U.S. Department of Transportation.

Morgan believes federal regulation of railroads must be continued to ensure fairness in rate-setting, in relations between large railroads and the new short and regional lines, and to resolve service problems.

"There is a lot of fear out there now," she said.

Although ICC officials believe approval or rejection of railroad mergers should remain with a regulatory body, officials at the justice and transportation departments think that general anti-trust laws are adequate to guard against anti-competitive activity.

Edwin Harper, president of the Association of American Railroads, said regulation of railroads, which began in 1887 when the ICC was created, became more onerous as railroads faced

increasingly heavy competition from trucks, barges and airlines after World War II.

For example, an attempt by the Union Pacific Railroad to buy the Rock Island Line was delayed for many years by the ICC until the issue was moot when the Rock Island went bankrupt. The ICC also prevented the Southern Railroad from lowering its rates by 40 percent for hauling grain and coal in giant new hopper cars.

Railroads are pushing Congress for minimal regulation from the DOT.

Harper told the House Transportation Committee, "There can be no doubt of the competitive nature of the marketplace in which railroads provide their services. . . . They compete with each other and with trucks and barges. They compete against other geographic sources or consuming points."

Harper said railroads are crucial in the ability of U.S. farmers to compete for business on world markets. The United States is the world's largest exporter of soybeans, even though soybeans often can be produced in Brazil cheaper than in the United States, he said.

"But U.S. farmers still beat the socks off Brazilian soybeans because of one fundamental fact: It costs Brazilians three to seven times more to get their beans from the field to the port," he said.

If railroads rates are too high, Harper said, "The railroad doesn't haul grain; there's no business; no revenue. We want the U.S. grain shippers to win in a competitive market. When they win, we win."

But he said some federal regulations hamper the ability of railroads to compete with other transportation modes. Railroads are required to give 20 days notice before they can change their rates, although barges are allowed to change their rates instantly.

A recent U.S. Department of Agriculture report said that problems in providing adequate rail service to grain shippers is largely related to railroads' inability to quickly adjust rates to reflect the true demand for their service.

Harper said that in spite of such regulatory inflexibility, railroads added 2,000 grain hopper cars during the first six months of 1995.

Railroads are like most other businesses, he said, and are

profit-driven. "Regulation doesn't create hopper cars or locomotives," he said. "Having a rate of return is what creates them."

- George Anthan

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Business

Rail mergers rattle shippers
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Washington News Bureau

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Washington, D.C. - For 15 years, six Montana farmers have been fighting the Burlington Northern Railroad, accusing the giant company of taking advantage of its dominance in Montana transportation by charging "unjust and unreasonable rates" for hauling wheat and barley.

Their case, McCarty Farms vs. Burlington Northern, still is being argued in the courts and before the Interstate Commerce Commission.

While the lawyers do battle, the dispute has come to symbolize the fears of shippers in Montana and elsewhere, including Iowa, about the potential impact on railroad customers as the nation's rail network becomes dominated by an ever-dwindling number of companies.

In Iowa, 28.5 million tons of farm and food products originating within the state are hauled annually by railroads. Iowa ranks 11th nationally in rail carloads handled and 14th in total tons carried by rail.

Most experts agree that the health of Iowa's farm economy depends significantly on effective rail service at reasonable rates. But the rail industry and its customers face uncertainties because of this year's mergers of railroading's giants.

In the western half of the U.S., the merged Burlington Northern-Santa Fe and the expected merger of the Union Pacific and Southern Pacific will leave the region with just two huge railroads. Some shippers fear that their dominance will revive an era of a century ago when railroad practices spawned the populist political movement and led to the United States' first attempt at

government regulation of an industry.

"In a nutshell, we're a one-railroad state, and our grain freight rates are the highest in the nation because there's no competition," said George Paul, executive director of the Montana Farmers Union.

Trucks, Barges

But the Association of American Railroads says that despite some disagreements over rates and service, railroads today face fierce and efficient trucking and barge competitors. Officials of the group say that far from trying to gouge customers, railroads have rebuilt their profits and competitiveness through efficiency and customer-friendliness.

"We get our heads beaten in every day by other modes of transportation," said Edwin Harper, president of the rail group.

Critics forget, "railroads only get revenues if they move something somewhere," he said.

Even as Congress heads toward eliminating the Interstate Commerce Commission, ensuring continued federal regulation of railroad rates and practices remains an objective of the National Grain and Feed Association, a group representing more than 1,000 companies that store, sell, process and export two-thirds of all U.S. grains and oilseeds.

Kendell Keith, president of the grain association, wants to continue the "minimal safeguards" the ICC now provides shippers.

"Agriculture is fundamentally different from most other industries," he said. "In other industries, if carriers make transportation terms or rates uneconomic, points of supply or manufacturing often can be shifted.

"No Choice" of Location

"Grain and oilseed shippers have no choice but to locate in areas where climate and soils permit profitable production. And since many rail grain shippers are captive to a single railroad,

we believe strongly that some continued regulation of rail grain traffic is necessary."

The late Edward Madigan, when he was secretary of agriculture during the Bush administration, said a major concern for the competitiveness of U.S. agriculture was whether the few railroads emerging from a wave of mergers could resist the temptation to extract unfair profits.

In an average year, according to the railroad association, about 25 percent of grain moves by truck, about 25 percent by barge and 50 percent by rail.

Impact on Prices

Even though farmers themselves rarely ship their commodities by rail, they have much at stake in railroad service and rates. The U.S. Department of Agriculture reported recently that increases in rail rates on farm shipments are "borne by U.S. producers through prices they receive for grain."

The USDA analysts said, "Such price increases reduce the competitiveness of U.S. grain . . . and make alternative sources more attractive to foreign buyers."

Keith, the feed and grain association executive, said areas of the Midwest and West with no economically viable access to barge transportation already face high rail rates. In some years, he said, those rates can amount to more than half the farm value of a bushel of grain.

"This transportation cost ultimately comes out of the farmers' pockets," said Keith. "They have to get their grain to market or it's worthless."

As federal regulation of railroads fades, "we put ourselves at the mercy of fewer and fewer carriers," Keith added.

Congress is moving to shift some regulatory functions of the ICC to the U.S. Department of Transportation as part of a plan to abolish the nation's oldest regulatory agency, which was established in 1887.

Russell Kocemba, transportation manager of General Mills Inc., told the U.S. House Transportation Committee this year that shippers do not want to return to the situation before 1980,

when
heavy-handed regulation of railroads by the ICC drove a number of
railroads close to bankruptcy.

Maintain Protections

But Kocemba added, "Just as we do not think the clock should be
turned back to the pre-deregulation era, we also do not believe that the protections that Congress carefully crafted . . . should
be repealed."

Kocemba noted that rivers freeze in the winter, making it impossible for barges to compete with railroads then, and even when rivers are navigable, they don't necessarily run where

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